

# EMBLAZE

2010 ANNUAL REPORT & ACCOUNTS

# EMBLAZE

## CONSOLIDATED FINANCIAL STATEMENTS AS OF 31 DECEMBER 2010

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## EXECUTIVE CHAIRMAN STATEMENT & REVIEW

On behalf of the Board of Directors (the “Board”), we are pleased to enclose the 2010 financial results of Emblaze Ltd. (“Emblaze”, “Company” or “Group”). 2010 has seen Emblaze streamline its operation and focus on its core competency in the software arena as well as simplify its organizational structure.

Emblaze’s mission is to advance its position as an international provider of technology solutions with a particular focus on the software sectors, while delivering long term value to shareholders.

The following sections reflect the position of the Company as at 31 December 2010.

### HIGHLIGHTS FOR THE PERIOD ENDING 31 DECEMBER 2010

Until November 2010, the Emblaze Group consisted of two main operating arms: Growth and Innovation. After the successful sale of all its holdings in Formula Systems (1985) Ltd. (“Formula”), Emblaze now consists of the Innovation arm which, which relates to research and development, production and marketing of technology and solutions for mobile handsets and products.

### FINANCIAL HIGHLIGHTS:

- Net income attributable to Company’s shareholders totaled \$28 million compared to a loss of \$9.1 million in 2009;
- Total net income per share to Company’s shareholders reached \$0.25, compared to a loss of \$0.08 per share in 2009;
- Positive net cash flow of \$137 million in 2010 compared to net decrease of \$14 million in cash in 2009;
- The Company’s subsidiary, Emoze Ltd., turned cash-flow positive as it expands its strategic deals and the licensing of its push-mail solutions;
- Continued strong cash position with cash and cash equivalents of \$144 million; and
- The financial statements for the presented periods include reclassifications with respect to the discontinued operations of Formula, ELSE and ZONE-IP.

### OPERATIONAL HIGHLIGHTS:

- On 26 November 2010, Emblaze announced the completion of sale of its entire holding in Formula for a total cash consideration of \$ 139,138,400. As a result, all Formula activity is presented as discontinued operations.
- Emoze Ltd., the Company’s subsidiary and a provider of push-mail technology, has continued to expand through licensing of its solutions to handset manufacturers, distributors and operators. In December 2010, Emoze signed a strategic deal with TCL Communication Technology Holdings Limited for the licensing of Emoze solutions to be embedded in TCL and

Alcatel handsets. Emoze has been cash-flow positive in 2010 and is expected to increase revenues in 2011.

- On 30 June 2010, Emblaze announced its decision to cease further investments towards manufacturing of the First ELSE™ mobile device by its subsidiary ELSE Ltd. This decision has dramatically reduced the Company's operational and development costs going forward;
- On 28 July 2010, Emblaze filed a complaint against Apple<sup>1</sup> Inc. for infringement of the Company's patent for media streaming technology and its use in Apple's iPhone<sup>1</sup>, iPod<sup>1</sup> touch and iPad<sup>1</sup> devices as well as its desktops and laptops.
- In February 2010, Emblaze notified Microsoft Corporation that Microsoft's Smooth Streaming<sup>2</sup> technology that enhances Microsoft software such as Windows 7 infringes Emblaze's patent for media streaming technology. Discussions between the two companies have so far not resulted with an understanding.
- The Group's UK subsidiary, Emblaze Mobility Solutions Limited ("Emblaze Mobility"), has won its legal claim in a UK Tribunal against the decision of HM Revenue & Customs ("HMRC") to withhold £8.8 million of VAT repayments. HMRC did not appeal but still refuses to fulfill the tribunal's decision. Therefore, Emblaze Mobility had to file to the High Court of Justice to order HMRC to pay. The Company estimates the net cash proceeds from this claim to be approximately \$ 7 million (having deducted legal and other expenses and third parties' share).

## OUTLOOK

The Company's management believes in Emoze's ability to substantially increase revenues through licensing deals with phone manufacturers to embed the Emoze solution on a large number of devices and through other deals with distributors, operators and enterprises. The potential of these licensing deals present an excellent opportunity to create shareholder value.

In addition, as previously announced, Emblaze is in the process of identifying suitable investments into solid businesses that can offer Emblaze the opportunity to drive revenues and achieve long-term sustainable growth. The Company is carefully managing its cash so as to be able to take advantage of opportunities in the market. We look forward to reporting on further progress in the coming months.

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<sup>1</sup> Apple, iPhone, iPod Touch and iPad are proprietary names of Apple Inc.

<sup>2</sup> IIS Smooth Streaming is a proprietary name of Microsoft Corporation

## INFORMATION ON THE COMPANY

Emblaze was incorporated in Israel on 19 January 1994. We maintain our principal executive offices at 9 Hamenofim Street, Herzeliya Pituach 46725, Israel and our telephone number is +972.9.7699333. Emblaze completed the initial public offering of its ordinary shares on the alternative investment market of the London Stock Exchange in October 1996 and thereafter completed a listing on the Official List of the London Stock Exchange in 1998.

Since our inception, we have acquired controlling interests, and have invested, in companies which are engaged in the IT, software and mobile solutions and services.

Historically, Emblaze's growth was organic as well as through mergers and acquisitions. We have adopted a strategy of seeking opportunities to realize gains through the selective investment in mature companies, as well as in innovative technologies that sit well alongside Emblaze's core competency and expertise in the IT and software arena. We believe that this strategy provides us with capital to support the growth of our operations, as well as increases value for our shareholders. We expect to continue to develop and enhance our in-house technology and solutions, and to pursue additional acquisitions of, or investments in, mature and established companies that provide IT services and proprietary software solutions.

Following the completion of the above measures, the Company's main innovation activity remains under EMOZE Ltd., a provider of push messaging solutions.

### EMOZE LTD.



Emoze Ltd., a 95 per cent. subsidiary of Emblaze, provides transparent, synchronized mobile push-messaging solutions that include email, PIM (contacts and calendar) and a push content platform for consumers, mobile operators, manufacturers and enterprises. Emoze eliminates the need for mobile devices to have check or poll servers, allowing for real-time messaging on a far wider range of mobile devices, including simple feature phones.

Emoze supports the leading operating systems (Android, Symbian, WindowsMobile and Java) and social communities. Synchronization and security are high priorities of customers and Emoze therefore seeks to deliver every email in the safest, most secure manner, employing compression and encryption to provide the highest level of security. In addition, Emoze never stores email on a third party server. Messaging is pushed only when the mobile device is open and ready to receive. Emoze push mail mobility is cost efficient as there is no need for the device to continuously poll the server. Email, events and attachments are pushed as they arrive and transmissions are optimized to conserve batteries and minimize data charges. Emoze transforms most low-end mobile devices into BlackBerry<sup>3</sup>-like devices, providing similar push mail, PIM and content service. Thanks to its novel and efficient technology, Emoze is able to provide a low-cost push solution for the mass market.

Emoze also provides solutions for enterprise communication needs. Its Enterprise server has additional layers of security by allowing the system administrator to control what information is synchronized between the corporate mail server and the employee's mobile device. This solution can allow the administrator to enable or disable synchronization of specific mail folders, send or receive email attachments, and even wipe the device remotely. The administrator can set

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<sup>3</sup> BlackBerry is a proprietary name of RIM

restrictions on a single device or create organization-wide policies for all the other company devices. All this and more can be easily managed from the user-friendly Emoze Enterprise system administration console.

Today, low-priced feature phones may have touch screens or QWERTY interfaces, but they are still limited in functionality. For these popular low-cost handsets, Emoze is able to offer a robust, push email service that delivers a true Smartphone-like experience.

Emoze is currently collaborating with handset manufacturers to pre-embed its proprietary push-mail application on a range of mobile devices, including feature phones such as MmediaTech and Qualcomm as well as Android Smartphones, enabling end-users to immediately access their email and PIM with no download or installation required. The end-user simply creates an account, by entering the email address and password once, and begins sending and receiving email and synchronizing his contacts and calendar.

Emoze's unique technology offers:

- Real-time notification on device desktop: when there is an event, the notification server wakes the Emoze application Java/Native or Android, notifies the device, and pushes the event either to or from the mobile device in real time.
- Safety and security of information: emails are never stored anywhere on any server. All data is compressed and encrypted during transfer and there is no need for further backup or storage.
- Low battery usage: the Emoze application stays idle until needed, saving money, battery power and data bandwidth
- Smart routing: no duplication of user's data
- Data compression for efficient data transfer and easier viewing
- Usability: transcodes attachments for easy viewing and minimize data bandwidth
- The ability to view office documents even when the mobile device does not have native viewer support

Emoze also provides solutions for enterprise communication needs. Its Enterprise server has additional layers of security by allowing the system administrator to control what information is synchronized between the corporate mail server and the employee's mobile device. This solution can allow the administrator to enable or disable synchronization of specific mail folders, send or receive email attachments, and even wipe the device remotely. The administrator can set restrictions on a single device or create organization-wide policies for all the other company devices. All this and more can be easily managed from the user-friendly Emoze Enterprise system administration console.

The Emoze Enterprise solution empowers business with a push email technology that enables employees to be more productive, while providing a totally secure solution that is simple for the IT department to deploy, maintain and control. Emoze for Enterprise takes the complexity, risk and cost out of staying connected. Emoze for Enterprise offers any business serious about increasing information access an award winning solution that offers the most flexibility along with the highest level of security and the lowest total cost of ownership.

2010 achievements include:

- In December 2010 Emoze announced a strategic world-wide agreement with TCL Communication Technology Holdings Ltd., to pre-embed the EMOZE push email solution on TCL and Alcatel branded mobile products. As part of the agreement, TCL Communication has placed a significant order to license the EMOZE push email solution. Emoze has already granted licenses to embed the Emoze solution on millions of TCL – Alcatel phones.

- In October 2010 Emoze announced the extension of its smart management tool to the mail functions and personal information management of iPhone<sup>1</sup> mobile devices in addition to the already existing support its Enterprise Server is providing for the WinMobile and Symbian mobile operating systems.
- In September 2010, the United States Patent Office has granted Emoze's patent number 7,797,273 named "System and Method for Reliable Symmetric Data Synchronization". The patent was filed in March 2006.
- During 2010, Emoze signed several licensing agreements with leading distributors in the Philippines, South America and India.
- Emoze is currently in advanced cooperation activity with some of the leading device manufactures to pre-embed its push mail solution on all their feature phones and Android devices with the potential to be embedded on dozens of millions devices

## BOARD OF DIRECTORS

### Naftali Shani, Executive Chairman

Naftali Shani (62) is one of the four founding partners of Emblaze. Prior to founding Emblaze, he served as general manager of Bartrade Ltd. (a subsidiary of Bank Leumi, one of Israel's leading banks), dealing with trade finance and counter-trade worldwide, and as general manager of the Israeli Chemical Company, Pazchem. Prior to this, Mr Shani was the treasurer and controller of the Israeli Prime Minister's Office.

### Guy Bernstein, Chief Executive Officer

*Retired on 17 February 2011*

Guy Bernstein (43) joined Emblaze as chief financial officer and member of the board of directors in April 2004. Mr. Bernstein was appointed chief executive officer of Emblaze in December 2006. Prior to joining Emblaze, Mr. Bernstein served as chief financial and operations officer of Magic Software Enterprises (NASDAQ: MGIC), a position he held since 1999. At Magic, Mr Bernstein's responsibilities included the overseeing of all finance operations, legal and M&A worldwide including, budget planning, sales forecasting, board and SEC reporting and investor relations. Guy played a key role in Magic's corporate second offering raising US\$100 million in 2000. He also acted as the interim CEO for Magic's subsidiaries: MSE Israel Ltd. and Coretech Consulting Group, turning them around to profitability. Guy joined Magic from Kost Forer Gabbay & Kasierer, a member of Ernst & Young Global, where he acted as senior manager from 1994 to 1997. Mr Bernstein is a certified licensed public accountant and holds a BA in accounting and economics from Tel-Aviv University. Mr. Bernstein acts as chief executive officer of Formula Systems (1985) Ltd. since January 2008.

### Ilan Flato, Non-Executive Director (A) (R)

Ilan Flato (55) joined the board of directors of Emblaze in April 2006. Until 2004, Mr. Flato served as the VP for planning, economics & online banking in United Mizrahi Bank and as the chief economist of the bank, where he was responsible for strategic & business planning and all aspects of online banking. Between 1992 and 1996, Mr Flato served as the economic advisor to the Prime Minister of Israel. His responsibilities included participation in government meetings, membership of the economic delegation to peace talks with the Palestinians in Paris and membership of the board of directors of EL-AL (Israel Airlines & Israel Aircraft Industry). Prior to this position, Mr. Flato served in the Treasury Office as the deputy director of the budget department, responsible for the budgets of various governmental offices. In addition, Mr. Flato served as a member of the board of directors of several government-owned companies. Mr Flato has a BA in economics and work relationships from the Tel-Aviv University and Master in Law from the Bar-Ilan University.

### Shimon Laor, Non-Executive Director

Shimon Laor (44) served as the chief financial officer of Emblaze until April 2000, also directing the operations and legal departments. Since then he has served as a non-executive director on the Emblaze board and has been engaged in private business initiatives. Mr Laor holds a non-executive director position in ZONE-IP Ltd., a 65 per cent subsidiary of the Company, and Formula Systems (1985) Ltd. Prior to joining Emblaze in August 1995, Mr Laor served as an economist at the Head Office of the Foreign Currency Division of the First International Bank in Israel.

### Zvi Shur, Non-Executive Director (A) (R)

Zvi Shur (75) joined the board of directors of Emblaze in September 2007. Until 2002, Mr Shur served as the General Manager of the Israeli Diamond Manufacturers Association, a position he had held since 1983. Between the years 1982 and 1983, Mr Shur served as the general controller of Tadiran, an electronics concern after serving in the Israeli Defense Force in a wide scope of duties for almost 30 years. His most recent post in the Israeli Defense Force was as head of the budget department at the Ministry of Defense and financial advisor to the Chief of Staff, with the



rank of Brigadier General. Between the years 1982 and 2005, Mr Shur served as non-executive director of over 20 Israeli companies engaged in a variety of businesses from manufacturing to finance. In 2003, Mr. Shur founded the Shur Zvi Consulting and is an active member of management of the Maccabia village and Maccabi World Union. Mr Shur holds a Bachelor of Science in electrical engineering and a Masters of Science industrial and management engineering

#### Nahum Admoni, Non-Executive Director (A) (R)

Nahum Admoni (82) joined the board of directors of Emblaze in September 2008. Mr. Admoni currently serves as director of Universe Security Group Ltd., a private company, a position he has held since July 2003. In addition, Mr. Admoni has served as a member of the Board of Governors of the Ben Gurion University since 1998. Between the years 1989 and 1994, Mr. Admoni served as the chief executive officer of Mekorot, the Israel National Water Company. Prior to this, Mr. Admoni served as the head of the Israeli Secret Intelligence Service between the years 1982 and 1989. Previous directorships held by Mr. Admoni include ECI Telecom Ltd., a NASDAQ traded company until September 2007, where he served as a director between May 1998 and September 2000, Sunfrost Ltd., listed on the Tel Aviv Stock Exchange, where he served as external director under the Israeli Companies Law between September 2005 and September 2008, Housing & Construction Holding Company Ltd., a member of the Arison Group and listed on the Tel Aviv Stock Exchange, where he served as a director between August 1996 and November 2006, Discount Investment Corporation Ltd., listed on the Tel Aviv Stock Exchange, where he served as external director under the Israeli Companies Law between December 1999 and December 2004, The Israel Electric Corporation Ltd., an Israeli government corporation listed on the Tel Aviv Stock Exchange, where he served as a director between July 2000 and August 2003, Mishkan Bank Ltd., a private bank, where he served as a director between March 2000 and August 2003 and Bank Hapoalim, where he served as a director between June 1998 and December 1999. Mr. Admoni holds a BA and MA in Political Science from the University of California in Berkeley.

#### Yuval Cohen, Non-Executive Director

Yuval Cohen (49) joined the board of directors of Emblaze in May 2009. Mr. Cohen is the founding and managing partner of Fortissimo Capital, an Israeli private equity investment fund. Prior to founding Fortissimo Capital, Mr. Cohen was a general partner at Jerusalem Venture Partners (JVP), an international venture capital firm with over \$650 million under management. Mr. Cohen serves as chairman of Soda Club Holdings Ltd., and has served on boards of numerous companies, including: Precise Software Solutions, Inc. (sold to Veritas Software Corporation. NASDAQ: PRSE), PowerDsine Ltd. (NASDAQ: PDSN; sold to Microsemi), T.square Inc. (sold to Globespan Inc. NASDAQ: GSPN), Sheer Networks (sold to Cisco, NASDAQ: CSCO), Teleknowledge Group (sold to MTS NASDAQ: MTSL), Celltick Technologies, and XMPie (sold to Xerox, NASDAQ: XRX), Telrad Networks Ltd and Nur Macroprinters (NASDAQ: NURM; sold to Hewlett Packard in 2008). Prior to joining JVP, Mr. Cohen held various executive positions in the Silicon Valley. Mr. Cohen was the vice president of business development and also served as the general manager of the licensing division at DSP Group, Inc. (NASDAQ: DSPG). In addition, Mr. Cohen served as the vice president of Marketing at VDOnet Corporation and as the assistant to the president of Intel Capital at Intel Corporation (NASDAQ: INTC). Mr. Cohen received an MBA from the Harvard Business School and a B.Sc. in Industrial Engineering from Tel Aviv University

#### Shmuel Barashi, Non-Executive Director

Shmoulik Barashi (49) joined the board of directors of Emblaze in May 2009. Mr. Barashi is a partner at Fortissimo Capital, an Israeli private equity investment fund. Prior to joining Fortissimo, Mr. Barashi was a senior partner in BDO Ziv Haft, one of the largest accounting firms in Israel. At BDO, Mr. Barashi specialized in corporate finance, initial public offerings, due diligence evaluations, deal structuring, business consultancy, auditing and tax (both international and local), and valuation analysis. Mr. Barashi managed the Jerusalem branch of BDO Israel. Mr. Barashi received an MBA from Hebrew University, an LLM from Bar Ilan University and a BA in economics

and accounting from Hebrew University. Mr. Barashi holds certification as a public accountant in Israel.

Hagit Gal, Executive Director

*Joined on 24 November 2010*

Hagit Gal (38) joined the Group in 1999 and is an integral member of the corporate management team. During her tenure at Emblaze, Ms. Gal has been actively involved in the Group's M&A and fund raising activities, leading several equity related transactions and managing acquisitions and disposals of privately held companies.

Ms. Gal currently serves Company Secretary of Emblaze, ensuring the Company's compliance with listing and regulatory requirements, and is also responsible for the Company's investor and public relations as well as human resources. Ms. Gal is a member of the Israeli Bar as a licensed advocate and holds an LLB in law.

Ruth Breger, Non-Executive Director

*Retired on 30 April 2010*

Ruth Breger (60) was deputy general manager of most of the subsidiaries of the Industrial Development Bank of Israel (IDBI) and General Manager of two of its subsidiaries, where she was responsible for the management of funds and development of new business. Currently, Breger practices as a Certified Public Accountant in Israel and acts as a consultant. She became a non-executive director of Emblaze in October 1996 and retired in September 2006.

**A** Member of the Audit Committee

**R** Member of the Remuneration Committee

## CORPORATE GOVERNANCE

Incorporated in Israel, Emblaze Ltd. ("Emblaze" or the "Company") is listed on the Official List of the London Stock Exchange. The Company's Board is committed to high standards of corporate governance and is accountable to the Company's shareholders for good corporate governance

This statement describes how the principles of corporate governance are applied to the Company and the Company's compliance with the provisions set out in Section 1 of the Combined Code on Corporate Governance published by the Financial Reporting Council.

### THE BOARD

The Board is responsible for the Company's corporate governance policy. It recognises the importance of high standards of integrity and consistently seeks to apply the provisions set out in the Code. The Board is responsible for the overall conduct of the group's business and has the powers, authorities and duties vested in it by and pursuant to the relevant laws of the State of Israel and the Articles of Association.

The Company is controlled through its board of directors whose main roles are to:

- create value for shareholders;
- provide leadership of the Company;
- approve the Company's strategic and operating objectives;
- consider, and if thought fit, to approve major acquisitions and disposals;
- provide treasury policies;
- provide group governance policies;
- ensure that the necessary financial and other resources are made available to the management to enable them to meet those objectives; and
- operate within a framework of effective controls which enables the assessment and management of principal business risks

The Board is responsible for approving overall Company strategy and financial policy, acquisition and investment policy and major capital expenditure projects. It also appoints and removes members of the board and board committees, reviews recommendations of the audit committee, remuneration committee and nomination committee, and the appointment of the independent auditor. It also reviews the financial performance and operation of each of the Company's businesses.

The Board sets the standards and values of the Company and much of this has been embodied in the Company's Code of Conduct and Ethics and Human Rights Policy which can be found on the Company's website, [www.emblaze.com](http://www.emblaze.com).

The Company's Code of Conduct and Ethics applies to all directors, officers and employees of the Company. The Company's Code of Conduct and Ethics contains provisions under which employees can report violations of company policy or any applicable law, rule or regulation. The current procedure provides for information to be given anonymously or by named employees under conditions of confidentiality. Those employees who come forward and give their name are assured that they will receive the full protection and no retaliation will take place.

During the year ended December 2010, the Board comprised the following members:

Mr. Naftali Shani, the executive chairman<sup>4</sup>  
Mr. Guy Bernstein, the chief executive officer<sup>5</sup>  
Ms. Hagit Gal, executive director<sup>6</sup>  
Mr. Shimon Laor, a non-executive director  
Mr. Ilan Flato, a non-executive director<sup>7</sup>  
Mr. Zvi Shur, a non-executive director  
Mr. Nahum Admoni, a non-executive director  
Mr. Yuval Cohen, a non-executive director  
Mr. Shmuel Barashi, a non-executive director  
Ms. Ruth Breger, a non-executive director<sup>8</sup>

The Company believes that it is essential to maintain a number of long serving directors who may serve for more than the ten year period recommended under the Code in order to provide continuous experience and knowledge. Accordingly, two of its Board members, Mr. Naftali Shani and Mr. Shimon Laor, have served for 16 and 10 years respectively. The Board is of the opinion that the three independent non-executive directors that serve on the Board, as outlined below, provide appropriate checks and balances to ensure a high level of governance.

Mindful of its prime objective to ensure the Company's ongoing orderly operation, the Board has resolved to appoint Mr. Naftali Shani as Executive Chairman of the Company with effect from conclusion of the annual general meeting, which took place on 24 November 2010. The Board is aware that the UK Corporate Governance Code requires that the roles of chairman and chief executive should not be exercised by the same person. The Board considers, however, that the appointment of Mr. Shani is a sensible and justified departure from the above principle. The Board does not intend this combination of roles to be permanent and believes that it will be in the best interests of the Company to split the roles as soon as reasonably possible having regard to the implementation of the Company's acquisition strategy. The Board also considers that the structure of the Group whereby its subsidiary, Emoze Ltd., is managed by a separate chief executive under the overall strategic leadership of the Board ensures a sufficient balance and a clear division of responsibilities at the various decision making levels of the Group.

The chairman is responsible for running the Board and ensures that all directors receive sufficient relevant information on financial, business and corporate matters to enable them to participate effectively in Board decisions.

Directors are subject to re-election at every annual general meeting (with the exception of the External Directors, as further described below). The Board has the power at any time, and from time to time, to appoint additional directors (either to fill any vacancy or as additional directors) provided that the number of directors does not exceed the maximum permitted in accordance with the Company's articles of association. In such cases, the newly appointed director holds office until the next annual general meeting of shareholders immediately following such appointment.

Each of the directors has a service agreement with the Company. Details of the terms of the service agreements are set out in the Report on Directors' Remuneration.

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<sup>4</sup> Mr. Shani was appointed executive chairman with effect from conclusion of the annual general meeting dated 24 November 2010.

<sup>5</sup> Mr. Bernstein retired from his position as CEO and remained a non-executive director of the board with effect from conclusion of the annual general meeting dated 24 November 2010. Mr. Bernstein stepped down from his position as a director of the Company on 17 February 2011.

<sup>6</sup> Joined the Board as executive director with effect from conclusion of the annual general meeting dated 24 November 2010.

<sup>7</sup> Also acts as the senior non-executive director

<sup>8</sup> Retired on 30 April 2010.

The performance of the Board is assessed by the Chairman and the strengths and weaknesses identified are discussed at meetings of the Board. Any improvements that are required are implemented based on these regular discussions.

Under the Israeli Companies Law 5759-1999 (the "Israeli Companies Law"), a person who lacks the necessary qualifications and the ability to devote an appropriate amount of time to the performance of his or her duties as a director shall not be appointed director of a publicly traded company. While determining a person's compliance with such provisions, the company's special requirements and its scope of business shall be taken into consideration. Where the agenda of a shareholders meeting of a publicly traded company includes the appointment of directors, each director nominee should submit a declaration to the company confirming that he or she has the necessary qualifications and that he or she is able to devote an appropriate amount of time to performance of his or her duties as a director. In the declaration, the director nominee should specify his or her qualifications and confirm that the restrictions set out in the Israeli Companies Law do not apply.

Under the Israeli Companies Law, if a director ceases to comply with any of the requirements provided in the Israeli Companies Law, such director must immediately notify the company, and his or her term of service shall terminate on the date of the notice.

On appointment, non-executive directors receive a range of information about the Company which aims to provide an understanding of the Company as a whole, including its strategy, structure, geographic spread of operations, financial position, markets, products, technologies and people, as well as their legal responsibilities as directors. There is in place a procedure whereby the directors may, in furtherance of their duties, take independent legal and financial advice, at the Company's expense.

The interests of the Directors and their immediate families, both beneficial and non-beneficial, in the ordinary shares of the Company at 31 December 2010 as reported to the Company by the respective director were as follows.

	Number of ordinary <u>shares</u>	% of issued and outstanding share <u>capital</u>
Naftali Shani	15,482,784	13.86%
Shimon Laor	100,000	0.09%
Guy Bernstein	268,045	0.24%

Total issued share capital of the Company as at 31 December 2010: 140,578,154

Total issued and outstanding share capital of the Company as at 31 December 2010: 111,755,932

## BOARD MEETINGS

The Board meets on a regular basis to discuss the overall direction and strategic plan of the Company. Ad hoc meetings may also be convened to deal with matters between scheduled meetings as appropriate. Prior to each Board meeting, each director receives background materials related to the matters for discussion at the meeting. Once a year, a budget is discussed and approved by the Board for the following year. All directors are properly briefed on progress with respect to matters discussed at Board meetings and further information requested by a director is made available.

It is expected that all directors attend Board and relevant Committee meetings, unless they are prevented from doing so by prior commitments. Directors leave the meeting where matters relating to them, or which may constitute a conflict of interest to them, are being discussed.

The table below shows the number of years directors have been on the Board and their attendance at scheduled Board meetings and at meetings of the Audit and Remuneration Committees during the year ended 31 December 2010:

Meetings held in 2010	Years on Board	Board 15	Audit 6	Remuneration 2
<u>Meetings attended:</u>				
Naftali Shani	16	15	n/a	n/a
Guy Bernstein	6.5	14	n/a	n/a
Hagit Gal	- (joined in November 2010)	1	n/a	n/a
Shimon Laor	10	14	n/a	n/a
Ilan Flato	4.5	13	6	2
Zvi Shur	3	14	5	2
Nahum Admoni	2	13	5	2
Yuval Cohen	1.5	14	n/a	n/a
Shmuel Barashi	1.5	15	n/a	n/a
Ruth Breger	- (retired in April 2010)	-	n/a	n/a

n/a = not applicable (where a director is not a member of a committee)

During the year, other directors have attended meetings of the audit committee by invitation. These details are not included in the table above. On the occasion when a director cannot attend a meeting, he or she will normally make his views on the agenda items known prior to the meeting to the chairman or to another director or, in respect of committee meetings, to the chairman of the respective committee.

## INDEPENDENCE & QUALIFICATION

The Code recommends that the board of directors of a listed company should include a balance of executive and non-executive directors (and, in particular, independent non-executive directors) such that no individual or small group of individuals can dominate the board's decision taking. The Code states that the board of directors should determine whether a director is independent in character and judgment and whether there are relationships or circumstances which are likely to affect, or could appear to affect, the director's judgment. The Board has considered the independence of its non-executive directors in line with the principles of the Code (section A.3.1) and, following careful consideration, assessed the independence of the non-executive directors as set out herein.

Pursuant to the Israeli Companies Law, companies incorporated under the laws of Israel whose shares have been offered to the public in or outside of Israel, are required to appoint at least two external directors who meet certain statutory criteria of independence, which are in line with the independence requirement under the Code. The Israeli Companies Law provide that a person may not be appointed as an external director if the person is a relative of the controlling shareholder of the company or if that person or his or her relative, partner, employer, another person to whom he or she was directly or indirectly subject, or any entity under the person's control, has, as of the date of the person's appointment to serve as external director, or had, during the two years preceding that date, any affiliation or one of certain other prohibited relationships with the company or any person or entity controlling (or relative of such controlling person), controlled by or under common control with the company (or, in the case of a company with no controlling shareholder, any affiliation or one of certain other prohibited relationships with a person serving as chairman of the board, chief executive officer, a substantial shareholder or the most senior office holder in the company's finance department). The term "affiliation" and the similar types of prohibited relationships include:

- an employment relationship;
- a business or professional relationship, even if not maintained on a regular basis (but excluding a de-minimis level relationship);
- control; and
- service as an office holder.

No person may serve as an external director if the person's position or other business activities create, or may create, a conflict of interest with the person's responsibilities as an external director or may otherwise interfere with the person's ability to serve as an external director or if the person is an employee of the Israel Securities Authority or of an Israeli stock exchange. A person may furthermore not continue to serve as an external director if he or she accepts, during his or her tenure as an external director, direct or indirect compensation from the company for his or her role as a director, other than amounts prescribed under the Israeli Companies Law regulations (as described below) or indemnification, the company's undertaking to indemnify such person, exemption and insurance coverage. If, at the time of election of an external director, all other directors who are not the company's controlling persons or their relatives are of the same gender, the external director to be elected must be of the other gender.

Pursuant to the Israeli Companies Law, all external directors must have accounting and financial expertise or professional qualifications, and at least one external director must have accounting and financial expertise. A director with "accounting and financial expertise" is a director that due to his or her education, experience and skills has a high expertise and understanding in financial and accounting matters and financial statements, in such a manner which allows him to deeply understand the financial statements of the company and initiate a discussion about the presentation of financial data. A director is deemed to have "professional qualifications" if he or she either (i) has an academic degree in economics, business management, accounting, law or public service, (ii) has an academic or other degree or has completed other higher education, all in the field of business of the company or relevant for his/her position, or (iii) has at least five years experience as either a senior managing officer in the company's line of business with a significant volume of business, a public office, or a senior position in the company's main line of business.

An external director may be removed from office only: (i) by a court, upon determination that the external director to be so removed ceased to meet the statutory qualifications for his or her appointment or if he or she violated his or her duty of loyalty to the company; (ii) by the same percentage of shareholders, acting through a shareholders meeting, as is required for his or her election, if the board of directors has determined that the external director to be so removed has ceased to meet the statutory qualifications for his or her appointment or violated his or her duty of loyalty to the company and has proposed the removal to the shareholders. Such determination by

the board of directors is to be made in the first meeting of the board of directors to be convened following learning of the said cessation or violation. An external director who ceases to meet the conditions for his or her service as such must notify the company immediately and such service shall cease immediately upon such notification.

The initial term of an external director is three years and may be extended by the general meeting of shareholders, for up to two additional three year terms.

The Board has determined that Mr. Ilan Flato and Mr. Zvi Shur have the requisite accounting, financial and professional expertise as required of external directors under the Israeli Companies Law. Mr. Zvi Shur was appointed for a first three-year term as an external director at the Company's annual general meeting held on 11 September 2007. The second external director is Mr. Ilan Flato, who was appointed for a first three-year term at the annual general meeting held on 20 April 2006 and a second three-year term at the annual general meeting held on 08 December 2009.

Each committee of a Company's Board is required to include at least one external director and the audit committee must include all of the external directors.

An external director is entitled to compensation as provided in regulations promulgated under the Israeli Companies Law and is otherwise prohibited from receiving any compensation, directly or indirectly, in connection with services provided as an external director or otherwise to the company

The executive chairman, Naftali Shani, one of the founding shareholders of Emblaze, holds approximately 14% of the issued and outstanding share capital of the Company and is therefore not considered under the Code to be independent. As explained above, the Board considers, that the appointment of Mr. Shani as an executive chairman is a sensible and justified departure from the Code's principles, specifically since the Board does not intend this combination of roles to be permanent and intends to split the roles as soon as reasonably possible having regard to the implementation of the Company's acquisition strategy.

The Board has determined that the non-executive directors, Ilan Flato, Zvi Shur and Nahum Admoni all meet the Code's independence requirements, as they are independent of the Company's executive management and free from any material business or other relationship with the Company (either directly or as a partner, shareholder or officer of an organisation that has a relationship with the Company). Accordingly, the Board believes that there are no such relationships that could materially interfere with the exercise of its independent judgment.

Shimon Laor holds Company share as well as options under the Company's share option plan. However, the Board believes that the modest number of shares that he holds does not affect his independence. Furthermore, the exercise price attached to his the options granted to him under the Company's share option plan is significantly higher than the share price at the time of grant and therefore present a performance criteria which is in line with shareholders interest.

Under the Israeli Companies Law, the board of directors of a publicly traded company is required to make a determination as to the minimum number of directors (not merely external directors) who must have accounting and financial expertise (according to the same criteria described above with respect to external directors under). In accordance with the Israeli Companies Law, the determination of the board should be based on, among other things, the type of the company, its size, the volume and complexity of its activities and the number of directors. Based on the foregoing considerations and in light of Emblaze's position as a holding company, the Board determined that the number of directors with financial and accounting expertise in the Company shall not be less than one. As described above, currently Mr. Ilan Flato and Mr. Zvi Shur have been determined by the Board to possess such accounting and financial expertise. It should be



noted that other Board members also possess relevant financial expertise, such as Mr. Laor and Mr. Barashi.

The Board is satisfied that there is sufficient independent representation on the Board.

## BOARD COMMITTEES

The Board has established Audit, Remuneration and Nomination Committees. The duties of these committees are set out in formal terms of reference and the Board is satisfied that these terms conform to best corporate governance practice. The terms of reference for all Board committees can be found on the Company's website at [www.emblaze.com](http://www.emblaze.com).

The Company Secretary is secretary to all Board committees.

### AUDIT COMMITTEE

Under the Israeli Companies Law, the audit committee must have at least three members, including all external directors, and neither the chairman of the board, nor any person who is employed by or provides services to the Company nor any person having control over the Company (or any relative of such control person) may be a member of the Audit Committee.

Under a recent amendment to the Israeli Companies Law, the audit committee of a publicly traded company must consist of a majority of independent directors. An "independent director" is defined as an external director and as a director who meets the following criteria:

- he or she meets the qualifications for being appointed as an external director, except for (i) the requirement that the director be an Israeli resident (which does not apply to companies whose securities have been offered outside of Israel or are listed outside of Israel) and (ii) the requirement for accounting and financial expertise or professional qualifications; and
- he or she has not served as a director of the company for a period exceeding nine consecutive years. For this purpose, a break of less than two years in the service shall not be deemed to interrupt the continuation of the service.

The foregoing amendment to the Israeli Companies Law further provides that a company may also elect to impose, via the adoption of a proposed set of corporate governance rules, certain independence requirements with respect to the composition of the board of directors as a whole. Those requirements, if undertaken by a company, mandate that (i) if the company has no controlling shareholder or no shareholder that holds at least 25% of the company's voting rights, most of the members of the board must be independent directors, whereas (ii) if the company has a controlling shareholder or a shareholder that holds at least 25% of the voting rights, then at least one-third of the directors need to be independent directors.

As of the date of this annual report, we have not elected to adopt these corporate governance rules. However, the Audit Committee comprises three independent non-executive directors: Ilan Flato who was appointed to the Committee in April 2006 and became chairman of the Committee in September 2007, Zvi Shur who was appointed in September 2007 and Nahum Admoni who was appointed in September 2008.

The Board has determined that all three members of the Audit Committee are independent for the purposes of the Israeli Companies Law as well as for the purpose of the Combined Code. The members bring wide-ranging financial, commercial and management experience to the work of the Audit Committee.

The chairman of the Committee, Ilan Flato, has previously held a number of senior financial management positions. Hence, as previously described, the Board has determined that Ilan Flato is a 'financial expert' as that term is defined under the Israeli Companies Law, having recent and relevant financial and accounting knowledge and experience.

The Audit Committee meets at least twice a year and on other occasions when circumstances require. The quorum for a meeting of the Committee is two members. The Company's financial team and representatives from the independent auditor and the internal auditor attend meetings under a standing invitation. The chairman of the Board and other directors are able to attend meetings of the Committee under the practice that any director may attend any meeting of a Committee of the Board, provided that they have no conflict of interest in respect of business to be discussed. The Company Secretary is secretary to the Committee. Five meetings were held during the year 2010.

In accordance with its terms of reference, the Audit Committee is required to oversee the relationship with the Company's external auditors, to review the Company's preliminary results, interim results and financial statements and to monitor compliance with statutory and listing requirements for any exchange on which the Company's shares are quoted. It reviews the Company's internal control and risk management as well as the Company's cash investment policy. The Audit Committee also review the arrangements by which the Company's employees may, in confidence, raise concerns about improprieties in matters of financial reporting and other matters (commonly referred to as "whistle-blowing" procedures).

The Code and the Israeli Companies Law require the Company to ensure a sound system of internal control to safeguard shareholders investments and the Company's assets. Such system should cover all material controls – financial, operational, compliance and risk management. To comply with this provision, the Board appointed an internal auditor, who is responsible for examination of the Company's internal controls and reviewing their effectiveness. All the recommendations provided by the internal auditor are presented to the Audit Committee for review and evaluation. The Audit Committee then recommends the required measures, if any, to the Board of directors for final decision and execution.

During 2010, the internal auditor reviewed the Company's IT operations and security procedures at the request of the Audit Committee.

## INTERNAL CONTROL

The Board is responsible for establishing and maintaining the Company's system of internal control and for reviewing its effectiveness. Such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives, and can only provide reasonable but not absolute assurance against material misstatement or loss.

In order to create an ongoing process to fulfill this responsibility, the Board has established a number of measures in order to identify, evaluate and manage the key financial, operating and compliance risks faced by the Group throughout the year and up to the date of the signing of the accounts. These measures are summarised below:

- The Board generally meets at least once a month and is responsible for the major business risks faced by the Company and for determining the appropriate course of action to manage those risks.
- The Company's non-executive directors meet together from time to time in the absence of management.
- The Board has a budgetary process in which the key risks faced by the Company are identified. Performance is monitored and relevant action taken through the monthly reporting to the Board of variances from the Budget, updated forecasts for the period together with information on the key risk areas.
- Capital expenditure is regulated by the budgetary process and authorisation levels. For expenditure beyond certain levels, detailed written reports have to be submitted to the Board.
- Responsibility levels are communicated throughout the Company, including delegation of authority and authorisation levels, segregation of duties and other control procedures. The

Audit Committee monitors controls which are in force and any perceived gaps in the control environment, and also considers and determines relevant action in respect of any control issues raised by the external auditors. The findings of the Audit Committee are communicated to the Board.

- The Board has established an ongoing process for identifying, evaluating and managing significant risks faced by the Group. A risk review report, which identifies key risks, the impact should they occur, and action being taken to manage those risks to the desired level, is produced annually and reviewed regularly to ensure relevant actions are taken and new risks evaluated by each business unit and by each Company divisional head. Proposed improvements to the way that risks are managed are also reported. It is designed to manage rather than to eliminate the risks inherent in achieving the Company's business objectives and can therefore provide only reasonable and not absolute assurance against material misstatement or loss.
- Detailed financial procedures are set out for operating division.

The Company's auditors are Kost Forer Gabbay & Kasierer, a member of Ernst & Young Global. For the year ended 31 December 2010, the Board of Directors of the Company has determined the audit remuneration of its auditors at a level of US\$80,000. In addition, the auditors were entitled to remuneration of approximately US\$70,000 in relation to non-audit consultancy, which was mainly for consultancy required in relation to the disposal of the Company's holding in Formula.

## REMUNERATION COMMITTEE

Under the Israeli Companies Law, at least one external director must be a member of the Remuneration Committee. The members of the Remuneration Committee of the Company are Ilan Flato, Zvi Shur and Nahum Admoni.

In accordance with its terms of reference, the Remuneration Committee approves the remuneration of all of the Company's senior executives and is responsible for making recommendations to the Board on the Company's framework of executive remuneration and for determining on behalf of the Board the remuneration package for each executive director.

The primary responsibilities of the Committee are to ensure:

- That individual pay levels for executive directors should generally be in line with levels of pay for executives in similar companies with similar performance achievement and responsibilities;
- That share option and bonus schemes should be set at a level that provides sufficient incentive to the executive to produce results that will reflect the board's expectations.
- That total pay and long term remuneration will be sufficient to retain executives;
- That aggregate pay for all executive directors is reasonable in light of the Company's size and performance.

The Company combines four main elements of the remuneration package for Executive Directors:

### A) Basic salary

An executive director's basic salary is normally reviewed annually, and paid as a fixed cash sum monthly. The Committee, in determining salary adjustments, considers increased responsibilities such as the size of the Group, individual performance and contribution, as well as market practices.

#### B) Social benefits (including pension arrangements):

The Company rewards executive directors with social benefits that are common in the local employment environment, and can confer tax benefits. These can include Pension Contributions, Education Fund contributions as detailed below, as well as availability of a Company car.

#### C) Annual bonus payments:

The directors believe that retaining a workforce which is motivated to achieve the Group's objectives is fundamental to its continued prosperity. Accordingly, executive directors are eligible to participate in a performance related annual bonus scheme. The maximum potential bonus for any individual, together with the associated performance measures and targets, is set by the Remuneration Committee and thereafter, approved by the Audit Committee and the Board.

In accordance with existing service contracts, Mr. Naftali Shani is entitled to an annual bonus in an amount to be determined by the Remuneration Committee and approved by the Board based on achievements of targets to be determined by the Board.

The Company has several key performance measures used internally to monitor and challenge performance and to assist investment decisions. The performance indicators include revenue, gross profit margin, net change in cash and income/loss per share to Company shareholders.

#### D) Share option incentives:

It is the policy of the Company to grant share options under its employee share option schemes to all of its full time employees and executive directors in a manner that is consistent with that of other similar companies with whom Emblaze competes for recruitment and retention of staff, and which incentivises and rewards loyalty and high performance.

Options to acquire the Company's shares are granted in addition to other forms of remuneration. The price at which shares may be acquired is the higher of the fair market value at the date of grant or the average of 30 days trading prior to the grant date. The exercise of options granted is generally phased over four years. The grant or exercise of options may be linked to performance criteria.

On June 28, 2001 the Company's shareholders approved the Company's Global Option Plan. The Company reserved 10,000,000 registered (i.e. authorised) but unissued ordinary shares of the Company for the purpose of this option plan. On June 9, 2003 the shareholders approved the consolidation of the Geo Interactive Media Group Ltd. 1999 Stock Option Plan ("1999 Plan") with the Emblaze Ltd. 2001 Global Stock Option Plan ("2001 Plan") so as to treat shares reserved for allotment under the 1999 Plan as being reserved for allotment under the 2001 Plan (but without prejudice to the actual terms and conditions of each grant previously made under the 1999 Plan). The reason for the consolidation was that, following the adoption of certain amendments to Israeli tax laws, rules and regulations, grants under the 1999 Plan did not comply with such amendments. Therefore, the available pool of options under the 1999 Plan was transferred to the 2001 Plan. On August 31, 2006 the Company's shareholders approved an additional reserve of 13,000,000 registered (i.e. authorised) but unissued ordinary shares of the Company for the purpose of the Global Option Plan. The Company's 2001 Global Stock Option Plan will lapse in June 2011.

The table below sets the number of options granted to Company employees during the year ended 2010:

Total number of options granted to employees	Exercise Price	Option Expiry	Vesting Schedule
150,000	£0.46	22 November 2020	4 annual equal installments

Eligibility for vesting of Company options is subject to meeting of certain performance criteria, which are usually linked to pre-defined annual financial objectives and to focus on the most

important measures of business success, while rewarding individuals for outstanding performance. In this way option based rewards seek to align the interests of shareholders and those eligible. The vesting schedule of the options is usually set for four years as of grant date, and provides the Company with an additional retention measure.

The remuneration of non-executive directors is determined by the entire Board. No director participates in Board discussions on, or votes on matters relating to, their own remuneration.

## EMPLOYEES

Emblaze's employees are located in Israel. Following the decision to discontinue the operations of our mobile division, ELSE Ltd., the disposal of ZONE-IP and the sale of our holding in Formula, the Group carefully monitors its overhead and employment expenditure to insure streamlined and efficient operation, both on the cost side and from a professional aspect.

With respect to our employees in Israel, Emblaze is subject to various Israeli labor laws and labor practices, and to administrative orders extending certain provisions of collective bargaining agreements between the Israeli General Federation of Labor ("Histadrut") and the Coordinating Bureau of Economic Organizations (the Israeli federation of employers' organizations) to all private sector employees. For example, mandatory cost of living adjustments, which compensate Israeli employees for a portion of the increase in the Israeli consumer price index, are determined on a nationwide basis.

Israeli law also requires the payment of severance benefits upon the termination, retirement or death of an employee. Emblaze meets this requirement by (i) contributing on an ongoing basis towards funds that combine pension, insurance and, if applicable, severance pay benefits and (ii) payment of differences, if applicable. The Company's contribution for all of its employees to pension funds and severance account, are in amounts of 5% and 8.33%, respectively, of the employees' salary. In addition, the Company contributes up to 2.5% of the employees' salary to disability insurance. In addition, Israeli employers and employees are required to pay specified percentages of wages to the National Insurance Institute. Other provisions of Israeli law or regulation govern matters such as the length of the workday, minimum wages, other terms of employment and restrictions on discrimination.

## NOMINATION COMMITTEE

The Board has established a Nomination Committee which leads the process for Board appointments and makes recommendations to the Board. Under the Israeli Companies Law, at least one external director must be a member of the Nomination Committee. The Board has resolved that the committee should comprise only of all independent directors. Therefore, since September 2008, the nomination committee is chaired by Zvi Shur and its other members are Ilan Flato and Nahum Admoni. The Nomination Committee's principal function is to regularly review the structure, size and composition of the Board (including the skills, knowledge and experience required of directors) and to make recommendations to the Board as to any changes required.

## STATEMENT BY THE DIRECTORS ON COMPLIANCE WITH THE PROVISIONS OF THE COMBINED CODE

The Directors are satisfied that the procedures in place throughout the year ensured full compliance with the internal control requirements of the Combined Code. The Directors are further satisfied that the Company has been in compliance with the provisions set out in the Code throughout the year.

## RELATIONS WITH SHAREHOLDERS

The Company places a high degree of importance on maintaining good relationships and communications with both institutional and private investors and ensures that shareholders are kept informed of significant Company developments.

The Company's website ([www.emblaze.com](http://www.emblaze.com)) contains up to date information on the Company's activities and published financial results.

The Company welcomes dialogue with its shareholders and communicates with them through timely announcements, its interim and annual reports and through the Company's website, which is regularly updated. Regular meetings are held with institutional investors and the Company encourages the direct approach of its senior management by shareholders for questions and clarifications on the Company's business activities. Further, as senior non-executive director, Ilan Flato is available to shareholders.

The Company's annual general meeting is also used as an opportunity to communicate with shareholders. All shareholders are encouraged to attend the Company's annual general meetings in order to take advantage of the opportunity to ask questions of the directors. Separate resolutions are proposed on each substantially different issue so that each receives proper consideration, including the approval of the annual report and accounts. Proxy votes are announced after each proposed resolution is voted on by a show of hands.

Notice of general meetings and related documentation are (subject to certain exceptions) sent to shareholders at least 35 days in advance of such meeting.

## SHAREHOLDERS RIGHTS

The Company's issued share capital is comprised of ordinary shares of NIS 0.01 each. The total issued share capital of the Company as at 31 December 2010 is 140,578,154 of which, 111,755,932 ordinary shares are outstanding.

## SHAREHOLDERS DUTIES

Under the Israeli Companies Law, a shareholder has a duty to act in good faith towards the company in which he holds shares and towards other shareholders and to refrain from abusing his power in the company. The Company's articles of association represent the rules of contract between the Company and its shareholders and among shareholders themselves.

## MAJOR SHAREHOLDINGS

Major shareholders and number of shares as notified to the Company by the respective shareholders under the Disclosure and Transparency Rules of the UKLA are set out in the table below:

Name	Number of Shares	% of total voting rights
Fortissimo Capital Management Ltd	17,966,558	16.08
Schroders plc	16,964,792	15.22
Naftali Shani	15,482,784	13.86
Donald L. Sturm & Sturm Family Foundation	9,900,797	8.86

## CORPORATE SOCIAL RESPONSIBILITY

Emblaze recognises the obligations it has towards those with whom it has dealings, including its staff, customers, suppliers, shareholders and the community as a whole. Given the Company's relatively low social and environmental impact, the Company believes that there are few risks to its short and long term value proposition arising from these matters. Whilst the Board considers that material risks arising from social, ethical, employment and environmental issues are limited, given the nature of the Company's business, policies have been adopted in key areas to ensure that such risks are limited. More information on the Company's approach to these matters can be found in the Company's Ethics and Environmental Policies, which are available on the Company's website at [www.emblaze.com](http://www.emblaze.com).

Although the Company is not a manufacturing industrial company, our activities do have an impact on the environment as a result of the use of electricity, generation of waste as well as business and local travelling. Emblaze endeavours to take steps to minimise the impact of the Company's operations on the environment in a responsible and appropriate manner with the aim to provide a safe and healthy workplace for all employees. As such, the main guiding principles of our policy focuses on minimising waste generation and preventing pollution, reducing energy consumption and encourage recycling. In leading general environmental good practice, Emblaze will:

- continue to comply with environmental laws, regulations and industry standards of the countries in which we conduct business;
- continue to maintain its offices "smoke-free". There are only restricted outdoor areas where employees may smoke;
- continually seek to improve its environmental performance;
- minimise the consumption of energy and water used in our facilities;
- reduce, re-use and, wherever is environmentally practicable, recycle consumables and dispose of non-recyclable items in an environmentally acceptable manner.
- where possible, procure resources and services from suppliers who have a sympathetic approach to the environment; and
- carefully plan the business flights of its staff in order to maximise utilisation of each travel.

## REPORT ON DIRECTORS' REMUNERATION<sup>9</sup>

This remuneration report is made by the Board for the year ended 31 December 2010. It has been prepared on its behalf and for its approval by the Remuneration Committee. The report, which complies with the Directors' Remuneration Report Regulations 2002, sets out how the principles of the Combined Code relating to Directors' remuneration are applied. The Remuneration Committee believes that the Company was compliant with the provision of the Combined Code relating to the Directors' remuneration throughout the period.

### POLICY ON EXECUTIVE DIRECTORS' REMUNERATION

The Company's executive remuneration policy is to set total remuneration at levels designed to attract, motivate and retain high quality executives of appropriate ability, experience and integrity to manage the affairs of the Company. In formulating its remuneration policy, the Remuneration Committee is mindful of the competitive pressures inherent in the sector in which it operates. It is the Company's policy that remuneration components, except base salaries which are determined in accordance with compared companies, are related to the financial performance of the Company. Each of the directors has a service contract with the Company, providing a notice provision of a maximum of six months.

### REMUNERATION OF EXECUTIVE DIRECTORS

Guy Bernstein, chief executive officer of the Emblaze as of December 2006 and until November 2010, was appointed in January 2008 to become chief executive officer of Formula, a subsidiary of Emblaze until November 2010, in parallel to his executive position with the Company. Due to the fact that the majority of Guy Bernstein's time and attention was devoted to Formula, his remuneration is borne by Formula since December 2008 in accordance with an agreement he has entered into with Formula. Therefore, from 2009 onwards, the Company did not bear any of the costs related to Guy Bernstein's employment as Company CEO, except for the options he was granted in the past, on which he continued to accrue vesting as long as he was a director of the Company, as determined in his respective option agreements. Mr. Bernstein retired from his position as CEO of Emblaze in November 2010, and thereafter he retired from his position as a director of the Company on 17 February 2011. According to his respective option agreements, Mr. Bernstein is eligible for exercise of vested options until August 2011.

### EXECUTIVE DIRECTORS - REMUNERATION PACKAGES FOR THE YEAR 2010

(IN THOUSANDS OF US\$)

Name	Salary	Bonus	Insurance and/ or pension plan	Educational fund	Other	Total
Naftali Shani	283	-	41	19	43	386
Hagit Gal	7	-	1	1	8	17

\*) Ms. Gal was appointed as a director of the Board as of 24 November 2010. The figures in the above table represent remuneration between 24 November and 31 December 2010 only.

<sup>9</sup> It should be noted that the Company is providing the Directors' Remuneration Report in compliance with the regulations of Listing Rule 9.8.8, although under Israeli law, Emblaze is not required to disclose the compensation of its senior management and directors on an individual basis.



## EXECUTIVE DIRECTORS - SHARE OPTIONS

### EMBLAZE STOCK OPTION PLAN

	Number of options	Exercise Price	Cancelled	Vested	Option Expiry	Vesting Schedule
Guy Bernstein	160,000	£1.1677	-	160,000	August 16, 2011	4 equal annual installments
	240,000	£1.422	-	240,000	August 16, 2011	4 equal semi-annual installments
	1,650,000	£0.755	-	1,340,625	August 16, 2011	Quarterly over a period of 4 years
Hagit Gal	1,600	£3.2	-	1,600	April 17, 2011	4 equal annual installments
	10,000	£3.2	-	10,000	April 17, 2011	4 equal annual installments
	10,000	£1.13	-	10,000	April 14, 2014	4 equal annual installments
	8,400	£1.422	-	8,400	Dec., 14, 2014	4 equal annual installments
	20,000	£0.7275	-	15,000	Sept., 05, 2017	4 equal annual installments
	150,000	£0.4597	-	0	Nov. 22, 2020	4 equal annual installments

### SUBSIDIARIES STOCK OPTION PLAN

	Granting Subsidiary	Number of options	Exercise Price	Vested	Option Expiry	Vesting Schedule
Naftali Shani	EMOZE Ltd.	1,080,000	\$0.163	1,080,000	Sept. 11, 2013	Fully vested as of Sept. 11, 2007

## REMUNERATION OF NON-EXECUTIVE DIRECTORS

The remuneration of the non-executive directors is set by the Remuneration Committee and approved by the Audit Committee and the Board of Directors, subject to the approval of the annual general meeting.

Non-executive directors are entitled to fees of £20,000 per annum, paid quarterly. These fees have been determined with reference to available information on the fees paid to non-executive directors in other companies of broadly similar size, market cap and complexity. Non-executive directors are also entitled to reimbursement of reasonable out-of-pocket expenses.

Non-executive directors have service contracts with the Company under which, each non-executive director is subject to re-election at each annual general meeting. The two external directors are appointed, as required by Israeli law, for a term of three years and may be appointed for one additional three-year term.

None of the directors is involved in any discussion with the Board or any committee of the Board relating to their own remuneration, nor do they participate in any vote on their remuneration by the Board or any committee of the Board.

## NON-EXECUTIVE DIRECTORS - SHARE OPTIONS

### EMBLAZE STOCK OPTION PLAN

	Number of options	Exercise Price	Cancelled	Vested	Option Expiry	Vesting Schedule
Shimon Laor	250,000	£1.075	-	250,000	Nov. 24, 2020	Fully vested as of Nov. 24, 2010

**REPORT OF INDEPENDENT AUDITORS****To the Board of Directors and Shareholders of****EMBLAZE LTD.**

We have audited the accompanying consolidated balance sheets of Emblaze Ltd. ("Emblaze" or "the Company") and its subsidiaries as of December 31, 2009 and 2010, and the related consolidated statements of operations, changes in equity and cash flows for each of the three years in the period ended December 31, 2010. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of certain subsidiaries for the years ended December 31, 2008 and 2009 which were sold during 2010 and included in discontinued operations, which statements reflects total assets constituting approximately 53% of total consolidated assets as of December 31, 2009. Those statements were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to the amounts included for those subsidiaries referred to above, is based solely on the reports of the other auditors.

We conducted our audits in accordance with United States generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits and the reports of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as of December 31, 2009 and 2010, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2010, in conformity with United States generally accepted accounting principles.

As discussed in Note 2(u) and 2(v) to the consolidated financial statements effective January 1, 2009, the Company changed its method of accounting for business combinations and of accounting for transactions with non-controlling interests.

**CONSOLIDATED BALANCE SHEETS****U.S. dollars in thousands**

	<b>December 31,</b>	
	<b>2009*</b>	<b>2010</b>
<b>ASSETS</b>		
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 7,348	\$ 144,173
Short-term investments (Note 4(a))	119	229
Restricted deposits (Note 4(b))	1,074	420
Trade receivables	147	-
Other receivables and prepaid expenses (Note 6)	794	955
Assets of discontinued operations (Note 3)	588,854	221
<u>Total</u> current assets	<u>598,336</u>	<u>145,998</u>
LONG-TERM RECEIVABLES AND INVESTMENTS (Note 7)	<u>238</u>	<u>-</u>
SEVERANCE PAY FUND	<u>385</u>	<u>335</u>
PROPERTY AND EQUIPMENT, NET (Note 8)	<u>75</u>	<u>44</u>
<u>Total</u> assets	<u>\$ 599,034</u>	<u>\$ 146,377</u>

(\*) Reclassified due to discontinued operations.

The accompanying notes are an integral part of the consolidated financial statements.

**CONSOLIDATED BALANCE SHEETS**

**U.S. dollars in thousands, except share and per share data**

	<b>December 31,</b>	
	<b>2009 *)</b>	<b>2010</b>
<b>LIABILITIES AND EQUITY</b>		
<b>CURRENT LIABILITIES:</b>		
Trade payables	\$ 334	\$ 341
Other payables and accrued expenses (Note 9)	1,184	4,278
Liabilities of discontinued operations (Note 3)	280,371	3,255
<u>Total current liabilities</u>	<u>281,889</u>	<u>7,874</u>
<b>LONG-TERM LIABILITIES:</b>		
Accrued severance pay	486	452
<u>Total long-term liabilities</u>	<u>486</u>	<u>452</u>
<b>COMMITMENTS AND CONTINGENT LIABILITIES (Note 10)</b>		
<b>EQUITY: (Note 11)</b>		
Equity attributable to the Company's Shareholders:		
Share capital:		
Ordinary shares of NIS 0.01 par value -		
Authorized: 200,000,000 shares at December 31, 2009 and 2010;		
Issued: 140,578,154 shares at December 31, 2009 and 2010;		
Outstanding: 111,755,932 at December 31, 2009 and 2010		
	416	416
Additional paid-in capital	469,562	469,844
Treasury stock, at cost	(75,555)	(75,555)
Accumulated other comprehensive income	6,924	-
Accumulated deficit	(284,961)	(257,123)
Total Company's Shareholders' equity	116,386	137,582
Non- controlling interest	200,273	469
<u>Total equity</u>	<u>316,659</u>	<u>138,051</u>
<u>Total liabilities and equity</u>	<u>\$ 599,034</u>	<u>\$ 146,377</u>

\*) Reclassified due to discontinued operation.

The accompanying notes are an integral part of the consolidated financial statements.

**EMBLAZE LTD. AND ITS SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF OPERATIONS**

**U.S. dollars in thousands, except share and per share data**

	<b>Year ended December 31,</b>		
	<b>2008 *)</b>	<b>2009 *)</b>	<b>2010</b>
Revenues	\$ -	\$ 266	\$ 629
Cost of revenues	<u>-</u>	<u>203</u>	<u>166</u>
Gross profit	<u>-</u>	<u>63</u>	<u>463</u>
Operating expenses:			
Research and development, net	1,620	1,396	1,482
Selling and marketing	1,128	1,248	849
General and administrative	<u>4,236</u>	<u>2,935</u>	<u>2,616</u>
Total operating expenses	<u>6,984</u>	<u>5,579</u>	<u>4,947</u>
Operating loss	(6,984)	(5,516)	(4,484)
Financial income (expenses) (Note 13(a))	(270)	619	701
Other income (expenses) (Note 13(b))	<u>(1,300)</u>	<u>47</u>	<u>(785)</u>
Loss before taxes on income	(8,554)	(4,850)	(4,568)
Taxes on income (Note 12)	<u>(1,132)</u>	<u>-</u>	<u>-</u>
Loss from continuing operations	(9,686)	(4,850)	(4,568)
Gain (loss) from discontinued operations, net (Note 3)	<u>(1,753)</u>	<u>18,254</u>	<u>40,843</u>
Consolidated net income (loss)	(11,439)	13,404	36,275
Less: net income from discontinued operation attributable to non-controlling interest	<u>15,625</u>	<u>22,510</u>	<u>8,437</u>
Net income (loss) attributable to Company's shareholders	<u>\$ (27,064)</u>	<u>\$ (9,106)</u>	<u>\$ 27,838</u>
Basic and diluted income (loss) per share to Company's Shareholders:			
From continuing operations	\$ (0.09)	\$ (0.04)	\$ (0.04)
From discontinued operations	<u>(0.16)</u>	<u>(0.04)</u>	<u>0.29</u>
Net income (loss) per share	<u>\$ (0.25)</u>	<u>\$ (0.08)</u>	<u>\$ 0.25</u>
Weighted average number of shares used in computing basic and diluted income (loss) per share	<u>111,522,295</u>	<u>111,755,932</u>	<u>111,755,932</u>

\*) Reclassified due to discontinued operations.

The accompanying notes are an integral part of the consolidated financial statements.

EMBLAZE LTD. AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

U.S. dollars in thousands

	Share capital	Additional paid-in capital	Treasury stock, at cost	Accumulated other comprehensive income (loss)	Accumulated deficit	Non- controlling interest	Total equity	Total comprehensive income (loss)
Balance as of January 1, 2008	\$ 416	\$ 470,891	\$ (76,433)	\$ 4,993	\$ (248,791)	\$ 208,602	\$ 359,678	-
Changes during 2008:								
Dividend to non-controlling interest shareholder's	-	-	-	-	-	(19,553)	(19,553)	-
Issuance of shares upon exercise of stock options	*) -	(803)	803	-	-	(3,609)	(3,609)	-
Purchase of treasury stock	-	-	(24)	-	-	-	(24)	-
Tax benefits related to exercise of options in a subsidiary	-	58	-	-	-	57	115	-
Share based compensation expense	-	570	-	-	--	263	833	-
Comprehensive loss:								-
Securities net	-	-	-	(961)	-	(394)	(1,355)	\$ (1,355)
Foreign currency translation adjustment	-	-	-	2,919	-	384	3,303	3,303
Net loss	-	-	-	-	(27,064)	4,806	(22,258)	(22,258)
Balance as of December 31, 2008	416	470,716	(75,654)	6,951	(275,855)	190,556	317,130	
Total comprehensive loss								<u>\$ (20,310)</u>
Changes during 2009:								
Decrease in the Company's holding in subsidiaries	-	(757)	-	-	-	1,716	959	
Dividend to non-controlling interest	-	-	-	-	-	(15,369)	(15,369)	
Non-controlling interests changes due to holding changes and exercise of put option	-	(595)	-	-	-	(2,937)	(3,532)	
Issuance of shares upon exercise of options	*) -	(99)	99	-	-	1,463	1,463	
Share based compensation expense	-	297	-	-	-	1,845	2,142	
Comprehensive loss:								
Unrealized loss from available-for-sale marketable securities, net	-	-	-	(260)	-	(102)	(362)	\$ (362)
Foreign currency translation adjustments	-	-	-	233	-	591	824	824
Net income (loss)	-	-	-	-	(9,106)	22,510	13,404	13,404
Balance as of December 31, 2009	<u>\$ 416</u>	<u>\$ 469,562</u>	<u>\$ (75,555)</u>	<u>\$ 6,924</u>	<u>\$ (284,961)</u>	<u>\$ 200,273</u>	<u>\$ 316,659</u>	
Total comprehensive income								<u>\$ 13,866</u>

\*) Represent an amount less than \$ 1

The accompanying notes are an integral part of the consolidated financial statements.

**CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY**

U.S. dollars in thousands

	Share capital	Additional paid-in capital	Treasury stock, at cost	Accumulated other comprehensive income (loss)	Accumulated deficit	Non- controlling interest	Total equity	Total comprehensive income
Balance as of December 31, 2009	\$ 416	\$ 469,562	\$ (75,555)	\$ 6,924	\$ (284,961)	\$ 200,273	\$ 316,659	
Changes during 2010:								
Sale of shares of subsidiaries	-	-	-	(6,924)	-	(208,287)	(215,211)	(6,924)
Share based compensation expenses of subsidiaries	-	-	-	-	-	46	46	
Share based compensation expenses	-	282	-	-	-	-	282	
Comprehensive income:								
Consolidated net income	-	-	-	-	27,838	8,437	36,275	\$ 36,275
Balance as of December 31, 2010	<u>\$ 416</u>	<u>\$ 469,884</u>	<u>\$ (75,555)</u>	<u>\$ -</u>	<u>\$ (257,123)</u>	<u>\$ 469</u>	<u>\$ 138,051</u>	
Total comprehensive income								<u>\$ 27,996</u>

The accompanying notes are an integral part of the consolidated financial statements.

**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands**

	<b>Year ended December 31,</b>		
	<b>2008 *)</b>	<b>2009 *)</b>	<b>2010</b>
<u>Cash flows from operating activities:</u>			
Consolidated net income (loss)	\$ (11,439)	\$ 13,404	\$ 36,275
Less - gain (loss) from discontinued operations	<u>(1,753)</u>	<u>18,254</u>	<u>40,843</u>
Loss from continuing operations	<u>(9,686)</u>	<u>(4,850)</u>	<u>(4,568)</u>
Depreciation	44	45	41
Impairment and amortization of marketable debt securities premiums and accretion of discounts, net	2,436	163	-
Share based compensation expense	570	297	282
Share based compensation expense of subsidiaries	49	78	46
Net loss (gain) on sales of marketable securities, decrease in value of marketable securities and changes in accrued interest, net	690	(91)	(240)
Decrease (increase) in trade receivables, other receivables and prepaid expenses	1,030	(180)	(5)
Increase (decrease) in trade payables, other payables and accrued expenses, accrued severance pay, net and other long term liabilities	230	(753)	2,978
Other	<u>-</u>	<u>(56)</u>	<u>85</u>
Net cash used in operating activities from continuing operations	(4,637)	(5,347)	(1,381)
Net cash provided by (used in) operating activities from discontinued operations	<u>26,392</u>	<u>40,434</u>	<u>(11,888)</u>
Net cash provided by (used in) operating activities	<u>21,755</u>	<u>35,087</u>	<u>(13,269)</u>

\*) Reclassified due to discontinued operations.

The accompanying notes are an integral part of the consolidated financial statements.



**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands**

	<b>Year ended December 31,</b>		
	<b>2008 *)</b>	<b>2009 *)</b>	<b>2010</b>
<u>Cash flows from investing activities:</u>			
Purchase of property and equipment	\$ (54)	\$ (15)	\$ (10)
Investment in (proceeds from) short-term bank deposits and short marketable securities and restricted deposits, net	(36)	(596)	834
Proceeds from sales, calls and maturity of marketable securities	14,554	1,390	58
Investment in long-term bank deposits, net	(1,600)	-	-
Proceeds from realization of investments	-	838	-
Proceeds from sale of Formula	-	-	139,138
Net cash provided by investing activities from continuing operations	12,864	1,617	140,020
Net cash used in investing activities from discontinued operations	(32,382)	(12,401)	-
Net cash provided by (used in) investing activities	(19,518)	(10,784)	140,020
<u>Cash flows from financing activities:</u>			
Short-term borrowing and bank credit, net	(5,000)	-	-
Purchase of treasury stock	(25)	-	-
Net cash used in financing activities from continuing operations	(5,025)	-	-
Net cash provided by (used in) financing activities from discontinued operations	(52,345)	(38,645)	10,074
Net cash provided by (used in) financing activities	(57,370)	(38,645)	10,074
Effect of exchange rate on cash	2,481	(237)	-
Net increase (decrease) in cash and cash equivalents	(55,133)	(14,342)	136,825
Cash and cash equivalents at the beginning of the year **)	174,849	122,197	7,348
Cash and cash equivalents at the end of the year **)	<u>\$ 122,197</u>	<u>\$ 107,618</u>	<u>\$ 144,173</u>

\*) Reclassified due to discontinued operation.

\*\*) Cash and cash equivalents as of 2008 and 2009 include Cash and cash equivalents of discontinued operations.

Cash and cash equivalents at the beginning of 2010 exclude cash and cash equivalents of discontinued operations.

The accompanying notes are an integral part of the consolidated financial statements.

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

**U.S. dollars in thousands**

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**NOTE 1:- GENERAL**

Organization and business:

Emblaze Ltd. ("Emblaze" or "the Company" or "the Group") is an Israeli corporation. The Company's shares are traded on the London Stock Exchange ("LSE") under the symbol BLZ.

Until November 2010, the Company consisted of two principal business segments, namely Growth and Innovation.

The Growth segment related to the development, production and marketing of information technology ("IT") solutions and services controlled under the Company's holding in Formula Systems (1985) Ltd., a NASDAQ and Tel Aviv Stock Exchange ("TASE") listed company, ("Formula"). Formula comprise the following subsidiaries:

Matrix IT Ltd. ("Matrix") (TASE: MTRX) is an integration and information technology services company. At December 31, 2009, Formula held 50.10% of the issued share capital of Matrix.

Magic Software Enterprises Ltd. ("Magic") (NASDAQ & TASE: MGIC) develops, markets and supports composite application development and deployment platforms with a service-oriented architecture (SOA), including application integration and business process management (BPM), with existing and legacy systems. As at December 31, 2009, Formula held 58.19% of the issued share capital of Magic.

Sapiens International Corporation N.V. ("Sapiens") (NASDAQ & TASE: SPNS) is a global provider of IT solutions that modernize business processes and enable insurance organizations and other companies to adapt quickly to changes. As at December 31, 2009, Formula held 70.40% of the issued share capital of Sapiens.

The Company sold its entire holdings in Formula in November 2010, (see note 3). The company currently operates only in one segment of operation, the Innovation.

The Innovation segment relates to research and development of technology for advanced wireless and cellular solutions and products. Currently, this segment includes EMOZE Ltd. ("EMOZE"). EMOZE. is a provider of Push email and Personal Information Management ("PIM") synchronization to mobile users. The service is provided globally and to any mobile device.

During 2010 the Innovation segment included the following additional subsidiaries:

ELSE Ltd. ("ELSE") a wholly owned subsidiary was engaged in the design of advanced mobile devices. The Company ceased further investments towards manufacturing of the First ELSE™ mobile device in June 2010 (see note 3).

**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands**

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**NOTE 1:- GENERAL (Cont.)**

ZONE-IP Ltd. ("ZONE-IP") a holding company for IP related technologies and holds Emblaze VCON Ltd. ("EVC"), a provider of wireless video communications technologies and conferencing solutions for operators and enterprise markets over IP networks. The Company sold its entire holdings in ZONE-IP in December 2010 (see note 3).

**NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES**

The consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles ("U.S. GAAP").

**Significant accounting policies relating to continuing operations:**

## a. Use of estimates:

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. The most significant assumptions are employed in estimates used in determining the amounts of goodwill and other intangible assets, legal contingencies, tax assets and tax liabilities, share-based compensation costs, financial instruments with no observable market quotes, as well as in estimates used in applying the revenue recognition policy. Actual results may differ from estimated results.

## b. Subsequent event

In May 2009 the Financial Accounting Standard Board ("FASB") issued Accounting standard codification ("ASC") 855 "subsequent events" amended in February 2010. ASC 855 establishes general standards of accounting for disclosure of events that occur after the balance sheet date but before financial statement are issued. The Company evaluated all events on transaction that occurred after December 31, 2010 up through March 23, 2011 the date of issuance of the financial statements. During this period no material subsequent events have occurred.

## c. Financial statements in U.S. dollars:

The Company's management believes that the U.S. dollar is the primary currency of the primary economic environment in which the Company and certain of its subsidiaries operate. Thus, the functional and reporting currency of the Company and certain of its subsidiaries is the U.S. dollar.

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

**U.S. dollars in thousands**

**NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

Accordingly, amounts in currencies other than U.S dollars have been translated as follows in accordance with ASC No. 830, "Foreign Currency Matters" (formerly SFAS 52, "Foreign Currency Translation"):

Monetary balances - at the exchange rate in effect on the balance sheet date.

Revenues and expenses - at the exchange rates in effect as of the date of recognition of the transaction.

All exchange gains and losses from the re-measurement mentioned above are reflected in the statement of operations in financial expenses (income), net.

d. Principles of consolidation:

The consolidated financial statements include the accounts of the Company and the subsidiaries in which the Company has a controlling voting interest. Inter-company balances and transactions have been eliminated upon consolidation.

The significant subsidiaries held directly by the Company as of the balance sheet date whose accounts are consolidated in continuing operations are:

	December 31,		
	2008	2009	2010
	% of outstanding share capital		
EMOZE	95	95	95

e. Cash equivalents:

Cash equivalents are short-term highly liquid investments that are readily convertible to cash with original maturities of three months or less at the date acquired.

f. Short-term bank deposits:

Short-term bank deposits are deposits with maturities of more than three months but less than one year. Short-term bank deposits are presented at their cost, including accrued interest.

**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands**

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**NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

## g. Marketable securities:

The Company and its subsidiaries account for investments in marketable debt and equity securities in accordance with ASC 320, "Investments - Debt and Equity Securities". Management determines the appropriate classification of its investments in debt and equity securities at the time of purchase and reevaluates such determinations at each balance sheet date.

In accordance with ASC 320, the Company and its subsidiaries have classified certain of their marketable debt securities as trading securities. Trading securities are held for resale in anticipation of short-term market movements. Under ASC 320, marketable securities classified as trading securities are stated at the quoted market prices at each balance sheet date. Gains and losses (realized and unrealized) related to trading securities, as well as interest on such securities, are included as financial income or expenses as appropriate. All investments in marketable debt and securities as of December 31, 2010 were classified as trading securities.

For equity and debt securities, the Company and its subsidiaries recognize an impairment charge when a decline in the fair value of its investments below the cost basis is judged to be other-than-temporary.

Factors considered in making such a determination include the duration and severity of the impairment, the financial condition and near-term prospects of the issuer, and the intent and ability of the Company and its subsidiaries to retain its investment for a period of time sufficient to allow for any anticipated recovery in market value.

For declines in value of debt securities, effective January 1, 2009, the Company and its subsidiaries apply an amendment to ASC 320. Under the amended impairment model, an other-than-temporary impairment ("OTTI") loss is deemed to exist and recognized in earnings if the Company and its subsidiaries intend to sell or if it is more likely than not that it will be required to sell, a debt security, before recovery of its amortized cost basis.

If the criteria mentioned above do not exist, the Company and its subsidiaries evaluate the collectability of the security in order to determine if the security is other than temporary impaired.

**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands**

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**NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

For debt securities that are deemed other-than-temporary impaired, the amount of impairment recognized in the statement of operations is limited to the amount related to "credit losses" (the difference between the amortized cost of the security and the present value of the cash flows expected to be collected), while impairment related to other factors is recognized in other comprehensive income.

Interest income resulting from investments in structured notes is accounted for under the provision of ASC 320-10-35, the retrospective interest method should be used for recognizing interest income.

h. Property and equipment:

Property and equipment are stated at cost, net of accumulated depreciation. Depreciation is calculated by the straight-line method over the estimated useful lives of the assets.

	<u>%</u>
Computers and peripheral equipment	6 - 33

i. Income taxes:

The Company and its subsidiaries account for income taxes in accordance with ASC 740, "Income taxes". ASC 740 prescribes the use of the liability method whereby deferred tax assets and liability account balances are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. The Company and its subsidiaries provide a valuation allowance, if necessary, to reduce deferred tax assets to their estimated realizable value.

Deferred tax assets are classified as current or non-current according to the expected reversal dates.

The Company utilizes a two-step approach for recognition and measurement of liability for uncertain tax positions accounted for in accordance with an amendment of ASC 740. The first step is to evaluate the tax position taken or expected to be taken in a tax return by determining if the weight of available evidence indicates that it is more likely than not that, on an evaluation of the technical merits, the tax position will be sustained on audit, including resolution of any related appeals or litigation processes. The second step is to measure the tax benefit as the largest amount that is more than 50% likely to be realized upon ultimate settlement. The Company accrues interest and penalties related to unrecognized tax benefits in its provision for income tax.

**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands**

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**NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

## j. Revenue recognition:

Revenues derived from direct software license agreements are recognized in accordance with ASC 985-605, upon delivery of the software when collection is probable, where the license fee is otherwise fixed or determinable, and when there is persuasive evidence that an arrangement exists.

In addition in certain of the Companies arrangements the Company sells services with the licensing of software, as well as supporting hardware. Revenues from software licensing, service and hardware are recognized ratably over the contract period.

Deferred revenue includes unearned amounts received from customers but not yet recognized as revenues.

## k. Concentrations of credit risks:

The majority of the Company and its subsidiaries' cash and cash equivalents and marketable securities are invested in dollar. The cash is deposited in major banks in Israel. Generally, these deposits may be redeemed upon demand and, therefore, bear low risk. The Company's marketable securities consist of corporate shares, collateralized debt obligation and structured note.

## l. Accounting for stock-based compensation:

The Company accounts for stock-based compensation in accordance with ASC 718, "Compensation - Stock Compensation".

The Company recognizes compensation expense for the value of equity based payments, which has straight-line vesting, over the requisite service period of each of the awards, net of estimated forfeitures. Estimated forfeitures are based on actual historical pre-vesting forfeitures.

**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands****NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

The Company estimates the fair value of stock options granted using the Binomial method option-pricing model. The option-pricing model requires a number of assumptions, of which the most significant are expected stock price volatility and the suboptimal exercise factor. Expected volatility was calculated based upon actual historical stock price movements over the most recent periods ending at the date of grant. The suboptimal exercise factor represents the influence on the period that the Company's stock options are expected to be outstanding and was determined based on past exercise employee behavior. The Company has historically not paid dividends and has no foreseeable plans to issue dividends. The risk-free interest rate is based on the yield from U.S. Treasury zero-coupon bonds with an equivalent term to the contractual life of the options.

The fair value of the employee stock options was based on the following assumption:

	<u>2010</u>
Expected volatility	69%-73%
Risk-free interest rate	1.08%-1.2%
Dividend yield	0%
Suboptimal exercise factor	1.5
Annual forfeiture rate	0-15%

No Options were granted in 2008 and an immaterial number of options were granted in 2009. During 2010 options were granted, please see note 11 (c).

m. Severance pay:

The Company and its Israeli based subsidiaries' liabilities for severance pay are calculated pursuant to Israeli Severance Pay Law based on the most recent salary of the employees multiplied by the number of years of employment, as of the balance sheet date. Employees are entitled to one month's salary for each year of employment or a portion thereof. The Company and its Israeli subsidiaries' liabilities for all of their employees are fully provided by monthly deposits with insurance policies and by an accrual.

The deposited funds include profits accumulated up to the balance sheet date. The deposited funds may be withdrawn only upon the fulfillment of the obligation, pursuant to Israeli Severance Pay Law or labor agreements. The value of the deposited funds is based on the cash surrender value of these policies, and includes immaterial losses.

The expenses in respect of severance pay for the years ended December 31, 2008, 2009 and 2010 were \$ 121, \$ 127, and \$ 226 respectively.



**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands**

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**NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

## n. Fair value of financial instruments:

The Company accounts for certain assets and liabilities at fair value under ASC 820, "Fair Value Measurements and Disclosures". Fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or a liability. As a basis for considering such assumptions, ASC 820 establishes a three-tier value hierarchy, which prioritizes the inputs used in the valuation methodologies in measuring fair value:

- Level 1 - Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets;
- Level 2 - Significant other observable inputs based on market data obtained from sources independent of the reporting entity;
- Level 3 - Unobservable inputs which are supported by little or no market activity (for example cash flow modeling inputs based on assumptions).

The fair value hierarchy also requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The Company categorized each of its fair value measurements in one of these three levels of hierarchy.

Assets and liabilities measured at fair value on a recurring basis are comprised of marketable securities, foreign currency forward contracts, and other derivative instruments (See Note 5).

The carrying amounts reported in the balance sheet for cash and cash equivalents, trade receivables, other receivable and prepaid expenses, short-term bank credit, trade payables and other accounts payable and prepaid expenses approximate their fair values due to the short-term maturities of such instruments.

## o. Basic and diluted net loss per share:

Basic and diluted net loss per share is computed based on the weighted average number of ordinary shares outstanding during each year.

**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands**

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**NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

## p. Comprehensive income (loss)

The Company accounts for comprehensive income (loss) in accordance with ASC 220, "Comprehensive Income". ASC 220 establishes standards for the reporting and display of comprehensive income and its components in a full set of general purpose financial statements. Comprehensive income (loss) generally represents all changes in equity during the period except those resulting from investments by, or distributions to, Shareholders. The Company determined that its items of comprehensive income (loss) relate to gain and loss on foreign currency translation adjustments and unrealized gain and loss on available-for-sale marketable securities. The Company total comprehensive income (loss) was realized in 2010 due to the sale of certain of the Company's subsidiaries (see note 3).

## q. Discontinued operations

Under ASC 205, "Presentation of Financial Statements - Discontinued Operation" when a component of an entity, as defined in ASC 205, has been disposed of or is classified as held for sale, the results of its operations, including the gain or loss on its disposal are classified as discontinued operations and the assets and liabilities of such component are classified as assets and liabilities attributed to discontinued operations; that is, provided that the operations, assets and liabilities and cash flows of the component have been eliminated from the Company's consolidated operations and the Company will no longer have any significant continuing involvement in the operations of the component.

## r. Treasury stock:

The Company repurchases its ordinary shares from time to time on the open market and holds such shares as treasury stock. The Company applies the "cost method" and presents the cost as a reduction in equity.

When treasury shares are reissued, the Company accounts for the re-issuance in accordance with ASC 505-30 "Treasury Stock (previously Accounting Principles Board No. 6) and charges the excess of the purchase cost over the re-issuance price (loss) to retained earnings. The purchase cost is calculated based on the weighted average method. In the event that the purchase cost is lower than the re-issuance price, the Company credits the difference to additional paid-in capital.

## s. Reclassifications:

Certain comparative figures have been reclassified to conform to the current year presentation.

**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands**

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**NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

## t. Adoption of new accounting policies:

- (1) ASU 2010-06 - In January 2010, the FASB updated the "Fair Value Measurements Disclosures" codified in ASC 820. More specifically, this update require (a) an entity to disclose separately the amounts of significant transfers in and out of Levels 1 and 2 fair value measurements and to describe the reasons for the transfers; and (b) information about purchases, sales, issuances and settlements to be presented separately (i.e. present the activity on a gross basis rather than net) in the reconciliation for fair value measurements using significant unobservable inputs (Level 3 inputs). This update clarifies existing disclosure requirements for the level of disaggregation used for classes of assets and liabilities measured at fair value, and require disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements using Level 2 and Level 3 inputs. As applicable to the Company, this update became effective as of the first quarter ended December 31, 2010, except for the gross presentation of the Level 3 roll forward information, which is required for annual reporting for 2010. The adoption of the new guidance did not have a material impact on the consolidated financial statements.
- (2) ASU 2010-09 - In February 2010, the FASB issued ASU 2010-09 - amendments to certain recognition and disclosure requirements of Subsequent Events codified in ASC 855. This update removes the requirement to disclose the date through which subsequent events were evaluated in both originally issued and reissued financial statements for "SEC Filers." Nevertheless it still requires the Company to evaluate subsequent events through the date that the financial statements are issued. The adoption of the new guidance did not have a material impact on the consolidated financial statements.
- (3) ASU 2009-13 - In October 2009, the FASB issued amendments to the accounting and disclosure for revenue recognition of multiple deliverable revenue arrangements codified in ASC 605-25. These amendments modify the criteria for recognizing revenue in multiple element arrangements and require companies to develop a best estimate of the selling price to separate deliverables and allocate arrangement consideration using the relative selling price method. Additionally, the amendments eliminate the residual method for allocating arrangement considerations. These amendments establish a selling price hierarchy for determining the selling price of a deliverable, which is based on: a) vendor-specific objective evidence; b) third-party evidence; or c) estimates. In addition, this guidance significantly expands required disclosures related to a vendor's multiple-deliverable revenue arrangements. ASU 2009-13 is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010, with early adoption permitted. The Company has not early adopted the guidance.

**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands**

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**NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)****u. Consolidation**

On January 1, 2009, the Company adopted an amendment to ASC 810, "Consolidation". According to the amendment, non-controlling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as a separate component of equity in the consolidated financial statements. As such, changes in the parent's ownership interest with no change of control are treated as equity transactions, rather than step acquisitions or dilution gains or losses. The amendment clarifies that losses of partially owned consolidated subsidiaries shall continue to be allocated to the non-controlling interests even when their investment was already reduced to zero.

The amendment applies prospectively, except for the presentation and disclosure requirements, which are applied retrospectively to all periods presented. As a result, upon adoption, the Company retroactively reclassified the "Minority Interests" balance previously included in a mezzanine section of the consolidated balance sheet to be presented in a new caption in total equity, "Non-controlling Interest". The adoption also impacted certain captions previously used on the consolidated statement of income, largely identifying net income including the portion attributable to non-controlling interest and net income attributable to the Company's shareholders. This amendment required the Company to classify non-controlling interest as part of the consolidated net income, and to include the accumulated amount of non-controlling interest as part of equity.

The net income amounts the Company has previously reported are now presented as "Net income attributable the Company's shareholders" and, as required, loss per share continue to reflect amounts attributable only to Emblaze's shareholders. Similarly, in the statements of changes in equity, the Company distinguishes between equity amounts attributable to the Company's shareholders and amounts attributable to the non-controlling interest.

**V. Business Combinations**

Effective January 1, 2009, the Company adopted the amended ASC 805, "Business Combinations" (formerly issued as FAS 141(R)). ASC 805 requires recognition of assets acquired, liabilities assumed, and non-controlling interest at the acquisition date, measured at their fair values as of that date. This ASC also requires the fair value of acquired in-process research and development ("IPR&D") to be recorded as intangibles with indefinite lives, contingent consideration to be recorded on the acquisition date, and restructuring and acquisition-related deal costs to be expensed as incurred. Any excess of the fair value of net assets acquired over purchase price and any subsequent changes in estimated contingencies are to be recorded in earnings. In addition, changes in valuation allowance related to acquired deferred tax assets and in acquired income tax position are to be recognized in earnings.

The ASC is applied prospectively for all business combinations occurring after January 1, 2009, except for changes in valuation allowance related to deferred tax assets and changes in acquired income tax position originating from business combinations that occurred prior to the effective date of this ASC, which are recognized in earnings following the adoption date.

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

U.S. dollars in thousands

**NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)****Significant accounting policies relating only to discontinued operations:****a. Marketable securities:**

The Company discontinued operation account for investments in marketable debt and equity securities in accordance with ASC 320, "Investments - Debt and Equity Securities". Management determines the appropriate classification of its investments in debt and equity securities at the time of purchase and reevaluates such determinations at each balance sheet date.

Debt and equity securities that are classified as available-for-sale are stated at fair value, with unrealized gains and losses reported in accumulated other comprehensive income (loss), a separate component of equity, net of taxes. Realized gains and losses on sales of investments, as determined on a specific identification basis, are included in the consolidated statement of operations.

**b. Provision for doubtful accounts:**

The provision for doubtful accounts is determined with respect to specific receivables, where, in the opinion of The Company discontinued operation ' management, their collectability is doubtful.

**c. Property and equipment:**

Property and equipment of discontinued operations are stated at cost, net of accumulated depreciation. Depreciation is calculated by the straight-line method over the estimated useful lives of the assets as follows:

	%
Computers and peripheral equipment	6 - 33
Buildings	2 - 4
Motor vehicles	15
Office furniture and equipment	6 - 15
Leasehold improvements	the shorter of the term of the lease or the economic life of the assets

**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands**

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**NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)****d. Income taxes:**

The Company discontinued operation account for income taxes in accordance with ASC 740, "Income taxes" ASC 740 prescribes the use of the liability method whereby deferred tax assets and liability account balances are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. The Company discontinued operation provide a valuation allowance, if necessary, to reduce deferred tax assets to their estimated realizable value.

Deferred tax assets are classified as current or non-current according to the expected reversal dates.

The Company utilizes a two-step approach for recognition and measurement of liability for uncertain tax positions accounted for in accordance with an amendment of ASC 740. The first step is to evaluate the tax position taken or expected to be taken in a tax return by determining if the weight of available evidence indicates that it is more likely than not that, on an evaluation of the technical merits, the tax position will be sustained on audit, including resolution of any related appeals or litigation processes. The second step is to measure the tax benefit as the largest amount that is more than 50% likely to be realized upon ultimate settlement. The Company accrues interest and penalties related to unrecognized tax benefits in its provision for income tax.

**e. Revenue recognition:**

Revenues derived from direct software license agreements are recognized in accordance with ASC 985-605, upon delivery of the software when collection is probable, where the license fee is otherwise fixed or determinable, and when there is persuasive evidence that an arrangement exists.

In addition there are certain arrangements where the Company sells software and consulting services. Consulting service fees are determined based on time invested.

The Company recognizes revenues from consulting fees with respect to projects billed on a time and material basis, based on the number of hours performed.

**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands**

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**NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

The Company recognizes revenues from projects of discounted operations as follows:

Revenue from projects billed on a time and material basis and from fixed fee contracts is recognized in accordance with ASC 605-35, "Construction-Type and Production-Type Contracts" (originally issued as SOP 81-1), using contract accounting on a percentage of completion method, on the basis of the relationship between actual costs incurred and the total costs that are expected to be incurred over the duration of the contract. Provision is made for estimated losses on uncompleted contracts in the period in which such losses first become evident.

Revenues from consulting services, consisting of billable hours for services provided, are recognized as the services are rendered.

Revenues from maintenance and training contracts are recognized ratably over the contract period.

Revenues from sale of hardware are recognized when the merchandise is delivered to the customer, provided no significant vendor obligations remain.

Some of the Company's contracts include client acceptance clauses. In these contracts, in determining when revenue can be recognized, when an acceptance clause exists, the Company considers, among other things, its history with similar arrangements, the customer's involvement in the progress, and the existence of other service providers and the payment terms.

There are no rights of return, price protection or similar contingencies in the Company's contracts.

Deferred revenue includes unearned amounts received under maintenance contracts and amounts received from customers but not yet recognized as revenues. Payments for maintenance fees are generally made in advance and are nonrefundable.

Tax collected from customers and remitted to government authorities (including VAT) are presented in statement of operation on a net basis.

f. **Concentrations of credit risks:**

The majority of The Company discontinued operation ' cash and cash equivalents and marketable securities are invested in dollar and in Shekels. The cash is deposited in major banks in Israel, Europe and the U.S. Deposits in the U.S. may be in excess of insured limits and are not insured in other jurisdictions. Generally, these deposits may be redeemed upon demand and, therefore, bear low risk. The Company's marketable securities consist of investment-grade corporate bonds, U.S. government agency securities, Sovereign bonds and structured notes.

**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands**

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**NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

The Company discontinued operation ' trade receivables are derived mainly from sales to large organizations located mainly in Europe, USA, North America, Far East and Israel. The Company discontinued operation performs ongoing credit evaluations of its customers and has established an allowance for doubtful accounts based upon factors relating to the credit risk of specific customers and other information. In certain circumstances, The Company discontinued operation ' may require letters of credit, other collateral or additional guarantees.

g. Severance pay:

The Company's Israeli discontinued operation liabilities for severance pay (for those who elected not to be included under section 14 of the Severance Pay Law -1963), are calculated pursuant to Israeli Severance Pay Law based on the most recent salary of the employees multiplied by the number of years of employment, as of the balance sheet date. Employees are entitled to one month's salary for each year of employment or a portion thereof. Company's Israeli discontinued operation liabilities for all of their employees are fully provided by monthly deposits with insurance policies and by an accrual.

The deposited funds include profits accumulated up to the balance sheet date. The deposited funds may be withdrawn only upon the fulfillment of the obligation, pursuant to Israeli Severance Pay Law or labor agreements. The value of the deposited funds is based on the cash surrender value of these policies, and includes immaterial losses.

Company's Israeli discontinued operation agreements with some of its employees, specifically state, in accordance with section 14 of the Severance Pay Law -1963, that the Company's Israeli discontinued operation contributions for severance pay shall be instead of severance compensation. Upon release of the policy to the employee, no additional liability exists between the parties regarding the matter of severance pay and no additional payments shall be made by the Company's Israeli discontinued operation to the employee.

h. Fair value of financial instruments:

The Company discontinued operation accounts for certain assets and liabilities at fair value under ASC 820, "Fair Value Measurements and Disclosures". Fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or a liability. As a basis for considering such assumptions, ASC 820 establishes a three-tier value hierarchy, which prioritizes the inputs used in the valuation methodologies in measuring fair value:



**CONSOLIDATED STATEMENTS OF CASH FLOWS**

U.S. dollars in thousands

**NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

- Level 1 - Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets;
- Level 2 - Significant other observable inputs based on market data obtained from sources independent of the reporting entity;
- Level 3 - Unobservable inputs which are supported by little or no market activity (for example cash flow modeling inputs based on assumptions).

The fair value hierarchy also requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The Company discontinued operation categorized each of its fair value measurements in one of these three levels of hierarchy.

Assets and liabilities measured at fair value on a recurring basis are comprised of marketable securities, foreign currency forward contracts, and other derivative instruments (See Note 5).

The carrying amounts reported in the balance sheet for cash and cash equivalents, trade receivables, other receivable and prepaid expenses, short-term bank credit, trade payables and other accounts payable and accrued expenses approximate their fair values due to the short-term maturities of such instruments.

**NOTE 3:- BUSINESS COMBINATIONS, SIGNIFICANT TRANSACTIONS AND SALE OF BUSINESSES**

Discontinued operations:

1. Orca Interactive Ltd. ("Orca"):

In March 2008, Viaccess S.A., a wholly owned subsidiary of France Telecom SA, entered into a merger agreement with Orca to acquire all of its shares.

The acquisition consideration consisted of an amount of \$ 13,000 plus Orca's net cash as of the closing, representing consideration of approximately \$ 12,900 for the Company.

On April 9, 2008, the Company increased its holding in Orca to 61.97%. The closing of the merger took place on May 19, 2008. As a result of the closing, the Company disposed of its entire holdings in Orca.

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

U.S. dollars in thousands

**NOTE 3:- BUSINESS COMBINATIONS, SIGNIFICANT TRANSACTIONS AND SALE OF BUSINESSES (Cont.)**

Accordingly, the Orca business has been treated as discontinued operations in the financial statements for 2008.

Summarized selected financial information of the discontinued operations of Orca is as follows:

	<b>Year ended December 31, 2008</b>
Revenues	\$ 2,296
Capital gains on disposal	\$ 5,539
Net income (loss) attributed to the Company's shareholders	\$ 2,862

2. Formula:

On November 26, 2010, the Company completed the sale of its entire holding in Formula to Asseco Poland SA. Ltd. for a total cash consideration of \$ 139,138.

Accordingly, the Formula business has been treated as discontinued operations in the financial statements for all periods presented. As of December 31, 2010 the Company has outstanding accrued expenses in the amount of \$1,950 related to this discontinued operation.

The carrying amounts of the major classes of assets and liabilities of Formula that have been reclassified as assets and liabilities of discontinued operations as of December 31, 2009, are as follows:

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

U.S. dollars in thousands

**NOTE 3:- BUSINESS COMBINATIONS, SIGNIFICANT TRANSACTIONS AND SALE OF BUSINESSES (Cont.)**

	<b>2009</b>
Current assets:	
Cash and cash equivalents, short-term deposit, and short-term marketable securities	\$ 158,214
Trade receivables	130,236
Other receivables and prepaid expenses	22,449
Inventory	2,439
Other assets	27
	<hr/>
Total current assets	313,365
	<hr/>
Long-term assets:	
Long-term investments and other long-term receivables	13,616
Property and equipment, net	9,989
Severance pay fund	44,131
Goodwill and other intangible assets	203,685
	<hr/>
Total long-term assets	271,421
	<hr/>
Total assets of discontinued operations	\$ 584,786
	<hr/>
Current liabilities:	
Trade payables	\$ 43,776
Other payables and deferred income	115,828
Other liabilities	314
	<hr/>
Total current liabilities	159,918
	<hr/>
Long-term liabilities:	
Accrued severance pay	53,893
Other long term liabilities	59,181
	<hr/>
Total long-term liabilities	113,074
	<hr/>
Total liabilities of discontinued operations	\$ 272,992
	<hr/>
Non-controlling interest	\$ 199,922
	<hr/>

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

U.S. dollars in thousands

**NOTE 3:- BUSINESS COMBINATIONS, SIGNIFICANT TRANSACTIONS AND SALE OF BUSINESSES (Cont.)**

Summarized selected financial information of the discontinued operations of Formula is as follows:

	<b>Year ended December 31,</b>		
	<b>2008</b>	<b>2009</b>	<b>2010*)</b>
Revenues	\$ 503,243	\$ 469,390	\$ 503,886
Net income attributable to the Company's Shareholders (*)	\$ 4,922	\$ 7,876	\$ 7,355
Capital gain on disposal			\$ 34,278

\*) Including amortization of Company's intangible assets in Formula. No tax expenses with respect to the gain for disposal was recorded as the Company offset its capital carry forward losses, of which full valuation allowance was provided, against such gain.

**3. ZONE-IP:**

In December 20, 2010 the Company decided to dispose of its entire holdings in ZONE-IP.

According to an agreement executed with Taltam Consulting & Investments Ltd., the Company assigned its entire holding in ZONE-IP, effective immediately.

Accordingly, the ZONE-IP business has been treated as discontinued operations in the financial statements for all periods presented. As of December 31, 2010 the Company has outstanding accrued expenses in the amount of \$495 related to this discontinued operation.

The carrying amounts of the major classes of assets and liabilities of ZONE-IP that have been reclassified as assets and liabilities of discontinued operations as of December 31, 2009 are as follows:

	<b>2009</b>
Current assets:	
Cash and cash equivalents, short-term deposit, and short-term marketable securities	\$ 125
Trade receivables	477
Other receivables and prepaid expenses	2,162
Total current assets	2,764
Long-term assets:	
Property and equipment, net	213
Severance pay fund	505
Goodwill and other intangible assets	199
Total long-term assets	917
Total assets of discontinued operations	\$ 3,681

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

U.S. dollars in thousands

**NOTE 3:- BUSINESS COMBINATIONS, SIGNIFICANT TRANSACTIONS AND SALE OF BUSINESSES (Cont.)**

	<b>2009</b>
Current liabilities	
Trade payables	\$ 718
Other payables and deferred income	2,299
Total current liabilities	3,017
Long-term liabilities:	
Accrued severance pay	734
Other long term liabilities	184
Liabilities	111
Total long-term liabilities	1,029
Total liabilities of discontinued operations	<u>\$ 4,046</u>

Summarized selected financial information of the discontinued operations of ZONE-IP is as follows:

	<b>Year ended December 31,</b>		
	<b>2008</b>	<b>2009</b>	<b>2010</b>
Revenues	<u>\$ 4,803</u>	<u>\$ 4,187</u>	<u>\$ 2,701</u>
Loss from disposal *)			<u>\$ (70)</u>

\*) Including loss attributed to the Company's Shareholders in 2010. Losses were not presented separately due to immateriality.

3. ELSE:

In June 2010 the Company decided to cease further investments towards manufacturing of the First ELSE™ mobile device by its subsidiary ELSE.

Accordingly, the ELSE business has been treated as discontinued operations in the financial statements for all periods presented.

The carrying amounts of the major classes of assets and liabilities of ELSE included as assets and liabilities of discontinued operations are as follows:

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

U.S. dollars in thousands

**NOTE 3:- BUSINESS COMBINATIONS, SIGNIFICANT TRANSACTIONS AND SALE OF BUSINESSES (Cont.)**

	<u>2009</u>	<u>2010</u>
Current assets:		
Other receivables and prepaid expenses	\$ 12	\$ 10
Total current assets	<u>12</u>	<u>10</u>
Long-term assets:		
Severance pay fund	327	184
Property and equipment, net	<u>48</u>	<u>27</u>
Total long-term assets	<u>375</u>	<u>211</u>
Total assets of discontinued operations	<u>\$ 387</u>	<u>\$ 221</u>
Current liabilities:		
Trade payables	\$ 1,442	\$ 16
Other payables and deferred income	<u>1,229</u>	<u>372</u>
Total current liabilities	<u>2,671</u>	<u>388</u>
Long-term liabilities:		
Accrued severance pay	<u>662</u>	<u>423</u>
Total long-term liabilities	<u>662</u>	<u>423</u>
Total liabilities of discontinued operations	<u>\$ 3,333</u>	<u>\$ 811</u>

Summarized selected financial information of the discontinued operations of ELSE is summarized in the table below:

	<b>Year ended December 31,</b>		
	<u>2008</u>	<u>2009</u>	<u>2010</u>
Net loss	<u>\$ (22,832)</u>	<u>\$ (10,595)</u>	<u>\$ (7,295)</u>

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

U.S. dollars in thousands

**NOTE 4:- SHORT-TERM INVESTMENTS AND RESTRICTED DEPOSITS**

- a. Short term investments and marketable securities:

	Interest rate December 31, 2010 %	December 31, 2009	December 31, 2010
Trading securities		\$ 39	\$ 229
Short-term deposits		80	-
Total		<u>\$ 119</u>	<u>\$ 229</u>

- b. Restricted deposits

The Company pledges bank deposits to cover bank guaranties in respect of an office rental agreement and a related party only in 2009.

**NOTE 5:- FAIR VALUE MEASUREMENTS**

The Company's financial assets measured at fair value on a recurring basis, excluding accrued interest components consisted of the following types of instruments as of December 31, 2009 and 2010:

	Fair value measurements using input type December 31, 2009			
	Level 1	Level 2	Level 3	Total
<b>Marketable securities:</b>				
Shares	\$ 39	\$ -	\$ -	\$ 39
<b>Long-term investments</b>				
Other marketable securities		137	-	-
<b>Total Financial Assets</b>	<u>\$ 39</u>	<u>\$ 137</u>	<u>\$ -</u>	<u>\$ 39</u>

	Fair value measurements using input type December 31, 2010			
	Level 1	Level 2	Level 3	Total
<b>Marketable securities:</b>				
Shares	\$ 9	\$ -	\$ -	\$ 9
Other marketable securities		220		220
<b>Total Financial Assets</b>	<u>\$ 9</u>	<u>\$ 220</u>	<u>\$ -</u>	<u>\$ 229</u>

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

U.S. dollars in thousands

**NOTE 6:- OTHER RECEIVABLES AND PREPAID EXPENSES**

	<b>December 31,</b>	
	<b>2009</b>	<b>2010</b>
Government authorities	\$ 33	\$ 41
Prepaid expenses and advances	492	737
Employees	206	31
Interest receivable	29	137
Other	34	9
Total	<u>\$ 794</u>	<u>\$ 955</u>

**NOTE 7:- LONG-TERM RECEIVABLE AND INVESTMENTS**

	<b>December 31, 2009</b>
Available for-sale marketable securities	\$ 137
Restricted deposits	101
Total	<u>\$ 238</u>

## a. Available for sale marketable securities

The following is a summary of marketable securities which are classified as available-for-sale marketable securities:

	<b>December 31, 2009</b>		
	<b>Amortized cost</b>	<b>Unrealized gain (loss)</b>	<b>Market value</b>
Marketable securities	\$ 137	\$ -	\$ 137
Total	<u>\$ 137</u>	<u>\$ -</u>	<u>\$ 137</u>

## b. Restricted deposits

	<b>Interest rate %</b>	<b>Linkage basis</b>	<b>December 31, 2009</b>
Restricted deposit	-	USD	\$ 101
Total			<u>\$ 101</u>



**CONSOLIDATED STATEMENTS OF CASH FLOWS**

U.S. dollars in thousands

**NOTE 8:- PROPERTY AND EQUIPMENT, NET**

	<b>December 31,</b>	
	<b>2009</b>	<b>2010</b>
Cost:		
Computers and peripheral equipment	\$ 234	\$ 243
Accumulated depreciation:		
Computers and peripheral equipment	159	199
Depreciated cost	\$ 75	\$ 44

Depreciation expense amounted to \$ 44 and \$ 45 and \$ 40 for the years ended December 31, 2008, 2009 and 2010, respectively.

**NOTE 9:- OTHER PAYABLES AND ACCRUED EXPENSES**

	<b>December 31,</b>	
	<b>2009</b>	<b>2010</b>
Employees and payroll accruals	\$ 761	\$ 1,180
Accrued expenses and other	296	355
Deferred income	127	2,743
	\$ 1,184	\$ 4,278

**NOTE 10:- COMMITMENTS AND CONTINGENT LIABILITIES**

## a. Liens:

The Company and some of its subsidiaries have liens on leased vehicles in favor of the leasing companies.

## b. Guarantees:

The Company and its subsidiaries have provided bank guarantees aggregating to \$ 320 as security for rent to be paid for their offices.

**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands**

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**NOTE 10:- COMMITMENTS AND CONTINGENT LIABILITIES (cont.)**

## c. Legal proceedings:

1. Emblaze Mobility Solutions Limited ("EMSL"), the Group subsidiary, is involved in a dispute with HM Revenue & Customs ("HMRC") regarding a decision made by HMRC to withhold Global Telecom Distribution Plc ("GTD") VAT reclaims and raise an assessment relating to GTD's VAT return in the sum of approximately £ 8,800,000, (which is an equivalent of \$ 13,620 as of December 31, 2010). These actions taken by HMRC were not specifically targeted at GTD but rather represent a part of general measures applied by HMRC in its battle against VAT fraud exposed within the mobile telephone handset sector in which GTD had operated. As a result of the action taken by HMRC, GTD ceased its business activities and an administrative receiver was appointed to GTD in May 2007. In 2010, the First-tier Tribunal ruled in favor of EMSL and ordered HMRC to pay EMSL the full value of input tax. HMRC did not appeal the First-tier Tribunal order but refused to pay EMSL as ordered. In 2011, EMSL has filed for Judicial Review in the High Court of Justice to order actual payment as ruled by the Tribunal. Due to the uncertainty regarding the final outcome of the legal proceedings, the Company has not recorded a receivable for the refund of input tax.
2. In November 2010, a claim was filed against the Company and its subsidiary, ELSE, in the Tel Aviv Labor Tribunal, claiming for termination indemnities in respect to an employment cessation of a former employee. The amount of the claim is NIS 2,700,000 (approximately \$ 492 as of December 31, 2010). The Company's management and legal advisors are of the opinion that there is no merit to the claim and the possibility that the claimant shall prevail is remote.
3. On 13 May 2010, ELSE filed a claim against one of its suppliers, ZETA Technologies Software Ltd. ("ZETA"), due to Zeta's failure to deliver the navigation system for the First ELSE handset that was ordered from it. The claim is for declaratory (prohibitive) judgment plus reimbursement of all the fees that were paid to ZETA (at the amount of ILS10,870,000). A prohibitive temporary injunction was granted on 16 May 2010 and the dispute was directed to arbitration. The arbitration expired on March 1st 2011 without resolution, and the Company now expects the claim to return to Court. Due to the uncertainty regarding the final outcome of the legal proceedings, the Company has not recorded a receivable for this claim.
4. At the request of the Administrator of former director, the Tel- Aviv District court issued an ex-parte temporary injunction on 06 September 2010, ordering the Company to withhold 27.75 percent of any dividend the Company may decide to distribute, to be held in trust by the Administrator General and Official Receivers Department of the Israeli Ministry of Justice. The Court clarified that any such amount belongs to all Company's Shareholders. Following an appeal filed by the Company, the Supreme Court cancelled the injunction on 29 November 2010, and limited the Company's responsibility only to notification obligation in case a decision on dividend distribution is made.

**CONSOLIDATED STATEMENTS OF CASH FLOWS**U.S. dollars in thousands

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**NOTE 10:- COMMITMENTS AND CONTINGENT LIABILITIES (cont.)**

5. The Company and/or its subsidiaries are involved in various legal disputes within the ordinary course of business. The Company's management is of the opinion that it had provided a sufficient reserve should any of these disputes materialize to actual claims

d. Lease commitments:

The Company rent its offices under operating lease agreements. Aggregate minimum rental commitments under non-cancelable leases as of December 31, 2010, are as follows:

2011	\$ 85
Total	<u>\$ 85</u>

Total rent expense for the years ended December 31, 2008, 2009 and 2010 amounted to \$ 330, \$ 350 and \$ 400, respectively.

**NOTE 11:- EQUITY**

a. Ordinary shares:

Ordinary shares confer upon their holders voting rights, the right to receive cash dividends, and the right to a share in excess assets upon liquidation of the Company.

b. Treasury stock:

1. During 2008, the Company repurchased a total of 63,800 of the Company's Ordinary shares in the open market at the cost of \$ 24.
2. During 2008 and 2009 the Company re-issued 305,545 and 37,500 held in treasury stock respectively as part of employees' exercise of options under the Company's employee option plan. (See also Note 11(c))

As of December 31, 2009 and 2010 the outstanding treasury stock amounted to 28,822,222 shares.

**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands**

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**NOTE 11:- EQUITY (Cont.)**

## c. Employee's stock option plans:

In 1998, the Company implemented the 1999 employee stock option plan ("the 1999 Plan"). Under the 1999 Plan, 12,000,000 options to purchase Ordinary shares have been reserved for issuance. These options may be granted to officers, directors and employees and vest evenly each year over a period of four years after the date of grant. If not exercised, the options will expire on the tenth anniversary of the date of grant. Generally the exercise price of granted options may not be less than the fair market price of the share at the date of grant. Any options that are either canceled or forfeited before expiration become available for future grants.

In 2001, the Company implemented the 2001 Global Stock Option Plan ("the 2001 Plan"). Under the 2001 Plan, 10,000,000 options to purchase Ordinary shares have been reserved for issuance. These options may be granted to the Company's employees, directors and consultants and vest evenly mainly either on an annual basis or semi-annual basis in equal portions over a period varying between two to four years, commencing on the date of grant. If not exercised, the options will expire on the tenth anniversary of the date of grant. Generally, the exercise price of these options may not be less than the fair market price of the shares at the date of grant. Any options that are either cancelled or forfeited before expiration become available for future grants.

On June 9, 2003, the Company's Shareholders approved the to consolidate the reserved Ordinary shares under 1999 Plan with the reserved Ordinary shares under 2001 Plan, so that shares reserved for allotment under the 1999 Plan will be treated as being available for allotment under the 2001 Plan, but without prejudice to the actual terms and conditions of each grant previously made under the 1999 Plan.

On August 31, 2006, the Company's Shareholders approved the increase of the reserve of stock for issuance under the Company's 2001 Plan by an additional 13,000,000 shares.

On September 11, 2007, the Company's Shareholders resolved to amend the Company's 2001 Plan such that the Board of Directors (the "Board") may grant employees of the Company options with an exercise price per share that is less than the fair market value of the shares on the date of approval of the grant, provided however that any such grant by the Board will be subject to the approval of the general meeting of Shareholders.

Total number of options available for future grants as of December 31, 2010, amounted to 20,387,557.

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

U.S. dollars in thousands

**NOTE 11:- EQUITY (Cont.)**

The following is a summary of the Company's stock options granted among the various plans:

	Year ended December 31,					
	2008		2009		2010	
	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
Outstanding at the beginning of the year	16,233,214	\$ 3.71	12,338,399	\$ 2.49	8,777,399	\$ 2.33
Granted	-	\$ -	15,000	\$ 0.79	400,000	\$ 0.84
Exercised	(305,545)	\$ -	(37,500)	\$ -	-	\$ -
Canceled or forfeited	(3,589,270)	\$ 3.66	(3,538,500)	\$ 3.84	(2,061,999)	\$ 2.30
Outstanding at the end of the year	<u>12,338,399</u>	<u>\$ 2.49</u>	<u>8,777,399</u>	<u>\$ 2.33</u>	<u>7,115,400</u>	<u>\$ 1.80</u>
Exercisable at the end of the year	<u>5,918,774</u>	<u>\$ 1.91</u>	<u>6,240,524</u>	<u>\$ 2.07</u>	<u>6,632,275</u>	<u>\$ 1.85</u>
Vested and expected to vest	<u>7,231,705</u>	<u>\$ 1.76</u>	<u>7,015,618</u>	<u>\$ 2.42</u>	<u>7,042,931</u>	<u>\$ 1.15</u>

The following table summarizes information about options outstanding and exercisable as of December 31, 2010:

Range of exercise price	Options outstanding as of December 31, 2010	Weighted average remaining contractual life (years)	Weighted average exercise price	Options exercisable as of December 31, 2010	Weighted average exercise price of options exercisable
\$ 0.000-1.926	2,597,600	6.09	\$ 1.310	2,114,475	\$ 1.38
\$ 2.014-2.918	4,476,600	2.56	\$ 2.056	4,476,600	\$ 2.06
\$ 4.377-3.121	20,000	4.25	\$ 3.310	20,000	\$ 3.31
\$ 4.669-5.326	<u>21,200</u>	0.23	\$ 4.953	<u>21,200</u>	\$ 4.95
	<u>7,115,400</u>		<u>\$ 1.80</u>	<u>6,632,275</u>	<u>\$ 1.85</u>

For options outstanding at December 31, 2010, the aggregate intrinsic value was \$ 8 and for options exercisable at December 31, 2010, the aggregate intrinsic value was \$ 0. The aggregate intrinsic value represents the total pre-tax intrinsic value based on the Company's closing stock price of \$ 0.76 on December 31, 2010, less the weighted average exercise price of in-the-money options. This represents the potential amount receivable by the option holders had all option holders exercised their options as of such date. The total intrinsic value of options exercised during the years ended December 31, 2008 and 2009 was \$ 120 and \$ 23, respectively.

The weighted-average grant-date fair value of options granted during the year ended December 31, 2010 was \$ 0.255. In 2009 the grant of options was immaterial.

**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands****NOTE 11:- EQUITY (Cont.)**

As of December 31, 2010, there was an unrecognized compensation cost of \$ 200 related to stock options that is expected to be recognized in future periods.

- d. Company subsidiary granted options to their employees to purchase shares in the respective company.

The options were mainly granted in the years 2008-2009. In general, the options are exercisable 1-4 years after the date of grant and expire 6-10 years after grant. Most of the options were granted as part of plans that were adopted in accordance with the provisions of Section 102 of the Israeli Income Tax Ordinance. The following table is a summary of the status of option plans the Company's subsidiaries as of December 31, 2010:

<b>Subsidiary</b>	<b>Outstanding options</b>	<b>Weighted average exercise price</b>	<b>Exercisable options</b>	<b>Weighted average exercise price of exercisable options</b>
EMOZE	<u>3,904,750</u>	<u>\$ 0.12</u>	<u>3,864,500</u>	<u>\$ 0.10</u>

- e. Grant of options to Non- executive Director and employees:
- On November 24, 2010 the shareholder of the Company approved to grant 250,000 share options to the Company's Non-executive Director, Mr. Shimon Laor. The exercise price of the stock options was determined at £ 1.075 while the fair market value of the shares at the date of grant was £ 0.485. The share options were fully vested immediately.
  - On November 22, 2010 the Board of the Company approved to grant 150,000 share options to the Company's employees. The exercise price of the stock options was determined at £ 0.46 while the fair market value of the shares at the date of grant was £ 0.453. The share options vest quarterly over a period of four years until November 2014.

**CONSOLIDATED STATEMENTS OF CASH FLOWS****U.S. dollars in thousands**

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**NOTE 12:- INCOME TAXES**

## a. Israeli income taxes:

## 1. Measurement of taxable income:

The Company measures its taxable income and file its tax return under the Israeli Income Tax Regulations (Principles Regarding the Management of Books of Account of Foreign Invested Companies and Certain Partnerships and the Determination of Their Taxable Income), 1986. Accordingly, results for tax purposes are measured in terms of earnings in dollar. The taxable income of certain subsidiaries is measured under the Income Tax (Inflationary Adjustments) Law, 1985. Accordingly, results for tax are measured and reflected in real terms in accordance with the change in the CPI. In February 2008, the "Knesset" (Israeli parliament) passed an amendment to the Income Tax (Inflationary Adjustments) Law, 1985, which limits the scope of the law starting 2008 and thereafter. Starting 2008, the results for tax purposes are measured in nominal values, excluding certain adjustments for changes in the Israeli CPI carried out in the period up to December 31, 2007. The amendment to the law includes, inter alia, the elimination of the inflationary additions and deductions and the additional deduction for depreciation starting 2008.

## 2. Tax rates:

The rate of the Israeli corporate tax is as follows: 2008 - 27%, 2009 - 26%, 2010 - 25%. Tax at a reduced rate of 25% applies on capital gains arising after January 1, 2003, instead of the regular tax rate.

In July 2009, the "Knesset" (Israeli Parliament) passed the Law for Economic Efficiency (Amended Legislation for Implementing the Economic Plan for 2009 and 2010), 2009, which prescribes, among others, an additional gradual reduction in the rates of the Israeli corporate tax and capital gains tax starting 2011 to the following tax rates: 2011 - 24%, 2012 - 23%, 2013 - 22%, 2014 - 21%, 2015 - 20%, 2016 and thereafter - 18%.

## b. Subsidiaries outside Israel:

Non-Israeli subsidiaries are taxed according to the tax laws in their respective domiciles of residence.

## c. Loss carryforward:

The Company and its Israeli subsidiaries have operating and capital accumulated losses for tax purposes as of December 31, 2010, in the amount of approximately \$ 184,507 which may be carried forward and offset against taxable income in the future for an indefinite period.

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

U.S. dollars in thousands

**NOTE 12:- INCOME TAXES (Cont.)**

The Company's foreign subsidiaries have accumulated losses for tax purposes as of December 31, 2010, in the amount of approximately \$ 5,200.

## d. Deferred taxes:

	<b>December 31,</b>	
	<b>2009</b>	<b>2010</b>
Operating and capital loss carryforward	\$ 56,149	\$ 34,769
Reserves and allowances	422	416
Net deferred tax asset before valuation allowance	56,571	35,185
Valuation allowance	(56,571)	(35,185)
Net deferred tax	<u>\$ -</u>	<u>\$ -</u>

The Company and its subsidiaries have provided valuation allowances in respect of deferred tax assets resulting from tax loss carryforwards and other differences. Management currently believes that since the Company and its subsidiaries have a history of losses it is more likely than not that the deferred tax regarding the loss carryforwards and other temporary differences will not be realized in the foreseeable future.

## e. Loss before taxes on income:

	<b>Year ended December 31,</b>		
	<b>2008</b>	<b>2009</b>	<b>2010</b>
Domestic	\$ 8,056	\$ 4,676	\$ 4,403
Foreign	498	174	165
Total	<u>\$ 8,554</u>	<u>\$ 4,850</u>	<u>\$ 4,568</u>

## f. Reconciliation of the theoretical tax expense to the actual tax expense:

The main reconciling item between the statutory tax rate of the Company and its subsidiaries and the effective tax rate are carryforward tax losses and other temporary difference for which a full valuation allowance was provided.



**CONSOLIDATED STATEMENTS OF CASH FLOWS**

U.S. dollars in thousands

**NOTE 13:- SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION**

- a. Financial income (expenses), net:

	<b>Year ended December 31,</b>		
	<b>2008</b>	<b>2009</b>	<b>2010</b>
Financial income:			
Interest, net	\$ 1,349	\$ 749	\$ 520
Net gain on marketable securities	344		113
Foreign currency translation differences, net	69	138	96
	<u>1,762</u>	<u>887</u>	<u>729</u>
Financial expenses:			
Interest and other bank charges	(674)	(158)	(23)
Foreign currency translation differences, net	(154)	(110)	(5)
Net loss on marketable securities	<u>(1,204)</u>		
	<u>(2,032)</u>	<u>(268)</u>	<u>(28)</u>
Total	<u>\$ (270)</u>	<u>\$ 619</u>	<u>\$ 701</u>

- b. Other income (expenses):

	<b>Year ended December 31,</b>		
	<b>2008</b>	<b>2009</b>	<b>2010</b>
Gain (loss) on realization of investments	\$ (1,270)	\$ 47	\$ -
Other *)	<u>(30)</u>	<u>-</u>	<u>(785)</u>
Total	<u>\$ (1,300)</u>	<u>\$ 47</u>	<u>\$ (785)</u>

\*) Malam Systems Ltd. claim against the Company and against its founding directors was settled between the parties and on July 7, 2010 the settlement was approved by the Court. According to the settlement, the Company contributed a one-time payment of \$ 1,000 to the overall agreed settlement. The Company recovered part of the payment from the Company's insurers in the amounted of \$ 215.

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